VIRGIN MONEY GROUP ANNUAL REPORT AND ACCOUNTS

2015

Virgin money

THERE'S MONEY AND THERE'S VIRGIN MONEY

At Virgin Money, our ambition is to build a bank that makes 'everyone better off'.

Customers, colleagues, communities, corporate partners and our company.

About us

With a powerful brand, strong balance sheet, customer-focused culture and experienced Executive Team, we have created a business which delivers our unique approach to banking and financial services to over three million customers.

Virgin Money Lounge, Haymarket, London

Table of contents

Cover image: Virgin Money Lounge, Haymarket, London

2015 Highlights

Results 2011-15		2015	2014	2013	2012	2011[1]
Growth						
Gross mortgage lending	£bn	**7.5**	5.8	5.6	4.9	3.7
Mortgage balances	£bn	**25.5**	21.9	19.6	16.8	13.9
Credit card balances	£bn	**1.6**	1.1	0.8	–	–
Deposit balances	£bn	**25.1**	22.4	21.1	18.0	16.2
Total assets	£bn	**30.2**	26.5	24.6	21.8	19.6
Quality						
Cost of risk	%	**0.12**	0.07	0.15	0.02	–
Common Equity Tier 1 capital ratio	%	**17.5**	19.0	15.5	15.5	18.7
Leverage ratio	%	**4.0**	4.1	3.8	3.6	4.0
Loan-to-deposit ratio	%	**107.5**	102.8	96.4	93.1	85.8
Returns						
Underlying total income	£m	**523.1**	438.2	361.5	234.6	161.7
Underlying profit/(loss) before tax	£m	**160.3**	104.8	40.0	(9.2)	(59.1)
Statutory profit before tax	£m	**138.0**	34.0	185.4	160.2	23.5
Underlying net interest margin	%	**1.65**	1.50	1.26	0.54	0.36
Underlying cost: income ratio	%	**63.6**	72.5	80.9	103.5	148.1
Underlying return on tangible equity	%	**10.9**	7.4	2.3	(1.1)	(5.2)
Underlying basic earnings per share	p	**26.7**	18.6	4.8	(1.8)	(21.1)

1 The 2011 results of Virgin Money Holdings (UK) plc have been presented as if Northern Rock plc had been part of the Group during 2011.

TOTAL CUSTOMER LOAN BALANCES GREW BY

18%

FULLY-LOADED COMMON EQUITY TIER 1 CAPITAL RATIO OF

17.5%

UNDERLYING PROFIT BEFORE TAX INCREASED 53% TO

£160.3 million

Results

These results have been prepared in accordance with International Financial Reporting Standards (IFRS). Where appropriate, certain aspects of the results are presented to reflect the Executive's view of the Group's underlying performance without distortions caused by non-recurring items that are not reflective of the Group's ongoing business activities. Underlying profit is now presented including the FSCS charge, as this is seen as an ongoing cost for the business. Prior periods have been adjusted. The Group's underlying results are presented on page 55 and a reconciliation of the Group's statutory and underlying results is reported on page 56.

In 2015, we delivered to all of our stakeholders, living up to our ambition to make everyone better off.

Highlights include:

CUSTOMERS

Overall Net Promoter Score increased to

+19

demonstrating continued focus and excellence in improving the experience, satisfaction and advocacy of over 3 million customers.

COLLEAGUES

Over

3,000

colleagues now work for Virgin Money, with an engagement score of 88%, up from 86% in 2014.

COMMUNITIES

Over

£92.5 million

was donated to charities in 2015, including Gift Aid, through Virgin Money Giving, our not-for-profit online donation service.

CORPORATE PARTNERS

Over

100,000

meetings held with our Intermediary Partners to support growth in our mortgage business. We were awarded the 'Best Lender for Partnership' at the L&G Mortgage Club annual awards.

COMPANY

Growth of

53%

in underlying profit before tax to £160.3 million, with underlying return on tangible equity increasing from 7.4% to 10.9%.

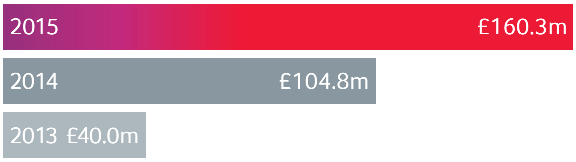
HRH Prince Harry and the VMLM 2015 Elite Women

2015 Highlights: Returns

All figures underlying unless stated

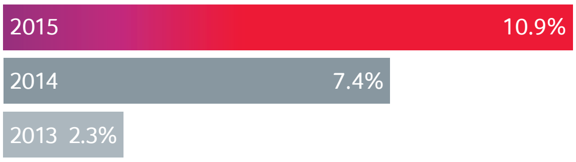
Profit before tax

53%
growth



Return on tangible equity

47%
growth



Statutory profit before tax

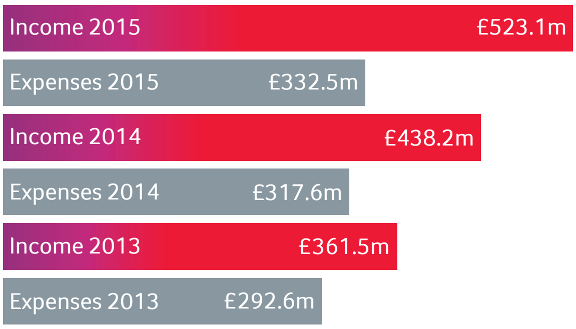
Statutory profit before tax was £138.0 million in 2015. This compares with a statutory profit before tax of £34.0 million in 2014.

Net interest margin

10%
growth

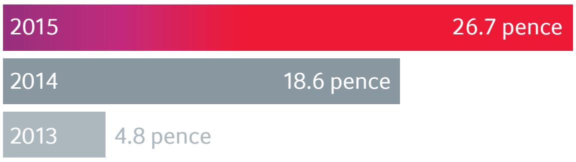
Operational leverage

19%
growth in total income 2014-15, against 5% expenses growth



Basic earnings per share

44%
growth



Final dividend

Recommended final dividend payment of 3.1 pence per ordinary share. This will result in a total dividend for 2015 of 4.5 pence per ordinary share.

2015 Highlights: Growth

STRONG ASSET GROWTH

	2015	2014
Mortgage balances up 16% to £25.5bn. Net lending of £3.6bn, a market share of 10.6%	**£25.5bn**	£21.9bn
Gross mortgage lending of £7.5bn, 29% higher than 2014. A full year market share of 3.4%	**£7.5bn**	£5.8bn
Credit card balances up 44% to £1.6bn, a market share of 2.5%	**£1.6bn**	£1.1bn

STRONG FUNDING POSITION

	2015	2014
Cash ISA balances up 45% to £10.7bn at the end of 2015	**£10.7bn**	£7.4bn
Other retail deposits reduced slightly as we focused on growing Cash ISA balances	**£14.4bn**	£15.0bn
Total deposit balances up 12% to £25.1bn, a market share of 1.5%	**£25.1bn**	£22.4bn
Wholesale funding up 36% reflecting continued diversification of funding base	**£3.3bn**	£2.4bn

Paula Radcliffe at the 2015 Virgin Money London Marathon

Quality

EXCELLENT ASSET QUALITY

	2015	2014
Mortgages over three months in arrears of 0.22% compared with latest industry average of 1.12%	0.22%	0.31%
Credit card balances two or more payments in arrears of 0.96% compared with latest industry average of 2.7%	0.96%	1.46%

COST OF RISK

	2015	2014
Low cost of risk continues to reflect strong asset quality	12bps	7bps

STRONG BALANCE SHEET POSITION

	2015	2014
Common Equity Tier 1 capital ratio of 17.5% compared with a fully loaded regulatory minimum of 7%	17.5%	19.0%
Leverage ratio of 4.0%, a level we believe to be conservative	4.0%	4.1%
Total capital ratio of 20.2%, as we continue to optimise our balance sheet within our prudent risk appetite	20.2%	22.1%

The 2015 Annual Report and Accounts incorporates the Strategic Report and the consolidated financial statements, both of which have been approved by the Board of Directors.

On behalf of the Board
Glen Moreno
Chairman
1 March 2016

2015 Virgin Money London Marathon finishers

Chairman's Statement

Glen Moreno Chairman

During 2015, our first full year as a listed business, we've taken the opportunity to review the Group's governance arrangements with a view to ensuring we can achieve our strategic objectives in the coming years.

Our customer-focused strategy, underpinned by our culture and strong corporate governance, provides the foundation that makes Virgin Money an attractive investment.

Given the performance of the business, which demonstrates the benefits of our unique position as a strong, low risk retail bank, and the strategic opportunities ahead of us, I believe we can look to the future with confidence.

The performance of the business in 2015 demonstrates the benefits of our unique position as a strong, customer-focused, low risk retail bank, unburdened by legacy conduct issues. During my first nine months as Chairman my colleagues have delivered on our strategy and the business has continued to perform well. We have delivered growth across our core mortgages, savings and credit card businesses, while maintaining our high-quality balance sheet, and generated significant growth in underlying profitability. I would like to extend my thanks to the Board, the management team and all colleagues across the Group for their contribution.

Our customer-focused strategy, underpinned by our culture and strong corporate governance, provides the foundation that makes Virgin Money an attractive investment. It enables the business to meet the challenges of an evolving regulatory and competitive environment and ensures the business continues to deliver sustainable success for all stakeholders.

As a result of the excellent performance of the business in 2015, including increasing our underlying profit before tax to £160.3 million, the Board has recommended a final dividend for 2015 of 3.1 pence per share which will, subject to shareholder approval at the 2016 Annual General Meeting (AGM), be paid in May 2016. Our objective is to increase dividend distributions over time as we grow our balance sheet and earnings.

As a UK retail bank we are focused on serving domestic customers and continue to support and benefit from the resilient UK economy and housing market. We anticipate that the UK economy will remain supportive of our business in 2016, to the extent that consumers continue to benefit from low interest rates, low inflation and low unemployment levels. We are however, very aware of the downside risks related to the impending UK referendum on EU membership, the uncertain outlook for interest rates, and the recent market turbulence caused by the slowdown in emerging markets and falling commodity prices, which could potentially have an adverse impact on the UK economy.

Given the recent trend of inflation being at or very close to zero, the timetable for UK rate rises continues to be pushed back. Indicators now suggest it could be some time before there is any upward movement in the official Bank Rate, currently at its historical low of 0.5 per cent.

During the year, there were significant developments in regulatory capital and liquidity requirements, including the introduction of the Basel III Liquidity Coverage Ratio, and the UK and European regulatory frameworks continue to evolve. We are compliant with current CRD IV/CRR requirements and we continue to work with the relevant authorities on the introduction of regulations connected to the Financial Services (Banking Reform) Act 2013. The Act will result in the ring-fencing of retail and commercial banking operations to separate them from investment banking activities. Given that we are a UK focused retail bank, we expect our entire business will be within the ring-fence when it comes into effect at the beginning of 2019.

Governance and Directors

We are committed to strong corporate governance and as a Board we rigorously challenge each other on strategy, performance, accountability and risk and control, to ensure that the decisions we make are of the highest quality.

During 2015, our first full year as a listed business, I took the opportunity to review the Group's governance arrangements, including Board composition and effectiveness, with a view to ensuring we can achieve our strategic objectives in the coming years. As a consequence of the review, there have been a number of changes to strengthen the team.

I am delighted that Peter Bole will join us as CFO in 2017, following which he will be appointed as an Executive Director. Peter is an accomplished professional with first-class strategic financial management experience. This appointment followed Lee Rochford's decision to leave the business in August 2015. We were also delighted to welcome Geeta Gopalan to the Board in June, as an Independent Non-Executive Director. Geeta's broad experience and knowledge of the financial services industry, including digital innovation, will be invaluable to us as we continue to grow the business. We appointed Marilyn Spearing as Chair of the Remuneration Committee following Olivia Dickson's announcement that she would retire from the Board on 31 December 2015. James B Lockhart III, WL Ross's nominee director, also stepped down as a Non-Executive Director of the Company in September, as a result of WL Ross, previously a controlling shareholder of the Group, reducing its shareholding. The Board recognises the significant contribution made by Olivia, Jim and Lee, and I would like to thank them for their contribution to the Group.

Colleagues and diversity

We have a strong, experienced management team and committed, engaged colleagues who are focused on delivering the needs of our customers and stakeholders. As a Board we believe that diversity helps to improve the quality of decision making and we are committed to increasing the diversity of independent Non-Executive Directors on the Board. As the Board evolves over time, diversity will remain a focus. Indeed, diversity at all levels of the business will be a priority in 2016, and in the years to come, as we continually strive to ensure that those who work for our business reflect the customers we serve, enabling us to provide a relevant, practical and personal banking service.

A responsible business

We are committed to supporting the communities in which we work, to help them flourish, both socially and economically. We remain dedicated to our charitable initiatives and I am delighted with the continued success of Virgin Money Giving, our not-for-profit online donation service. £92.5 million, including Gift Aid, was donated to charities through Virgin Money Giving in 2015.

In August, we launched the Virgin Money Foundation (the 'Foundation') – a new, independent charitable foundation that will focus initially on community projects in the North East of England, and over time will grow to operate nationally. We were delighted that the Government committed £4 million of funding – £1 million per year for four years – which Virgin Money will match. The Foundation will promote the sustainable regeneration of economically and socially deprived communities in the UK and will include social investment in community housing and building projects, promoting opportunities for youth work and training, as well as investing in projects designed to relieve unemployment.

We are committed to working responsibly with all of our stakeholders and look to partner with businesses that genuinely understand and share our philosophy of making 'everyone better off'. As a result, we are very supportive of The Modern Slavery Act 2015 and we will report against our progress in our 2016 Annual Report.

Remuneration

Our remuneration structure, at all levels, is designed to ensure rewards are aligned with the long-term success of the business and the interests of our shareholders. Variable pay for Senior Executives is delivered through a combination of annual bonus and a Long Term Incentive Plan linked to future business performance (both with appropriate deferral). All deferred awards are subject to a further risk assessment before release, with clawback provisions applying thereafter. In total, the 2015 variable pay pool represented 14 per cent of pre-bonus profit before tax. More information on how we ensure our approach to remuneration supports the business strategy can be found in our remuneration report on page 111.

Chairman's Statement

Looking ahead

Our business model and strategy give us the flexibility to continue to deliver for shareholders in the face of the changing economic and competitive environment, as well as the evolving regulatory regime. It will be important to adapt continually to the changing landscape of the future, including the digital transformation of UK retail banking.

As a Board, we have assessed the viability of the business over a three year period. Based on this assessment, including the results of our stress testing, we believe we are very well placed to make the most of the opportunities that exist and we can look to the future with confidence.

I am delighted to welcome the increasing number of retail and institutional shareholders investing in Virgin Money and look forward to engaging with shareholders over the course of 2016.

I would like to reiterate my thanks to my fellow Board members, the senior leadership team and all colleagues for their contribution to everything we have achieved together in 2015.

Glen Moreno
Chairman
1 March 2016

Virgin Money Lounge, Glasgow

Chief Executive's Review

Jayne-Anne Gadhia CBE Chief Executive

2015 has been a very successful year for Virgin Money and we are delighted that we continue to deliver strongly against our objectives.

Despite pressure on returns from the sustained low interest rate environment, we increased our underlying profit by 53 per cent to £160.3 million.

Our core mortgages and savings business performed strongly in 2015. We delivered growth in our mortgage book of 16 per cent, significantly exceeding market growth as we continued to support the UK housing market.

Following the successful migration of credit card accounts to our own platform, we grew balances ahead of expectations and are in a strong position to grow to our target of £3 billion by the end of 2017, a year earlier than planned. Growing the credit card business will enable us to achieve a more efficient use of our capital.

Results overview

2015 has been a very successful year for Virgin Money and we are delighted that we continue to deliver strongly against our objectives.

Despite pressure on returns from the sustained low interest rate environment, we increased our underlying profit by 53 per cent to £160.3 million. On a statutory basis, we delivered a profit before tax of £138.0 million, compared to £34.0 million in 2014.

On an underlying basis, our total income grew by 19 per cent to £523.1 million, driven mainly by strong growth in our lending and a 15 basis point increase in our net interest margin to 1.65 per cent. Our total costs increased by only 5 per cent to £332.5 million. During the year, the cost of risk was 12 basis points and the total impairment charge increase to £30.3 million, from £15.8 million in 2014, reflected growth in customer balances. Our underlying return on tangible equity improved from 7.4 per cent to 10.9 per cent.

We continue to manage our balance sheet within our prudent risk appetite with a view to maintaining its quality and efficiency. At the end of the year, our Common Equity Tier 1 (CET1) ratio was 17.5 per cent, our total capital ratio was 20.2 per cent, and our leverage ratio was 4.0 per cent. Our Liquidity Coverage Ratio was 202 per cent and loan-to-deposit ratio was 107.5 per cent at 31 December 2015.

Delivering growth

Mortgages

The UK mortgage market was very competitive in 2015, with total lending of just over £220 billion, marginally higher than the market had anticipated. We delivered strong gross mortgage lending of £7.5 billion, 29 per cent higher than in 2014. Over the year we achieved 16 per cent growth in mortgage balances to £25.5 billion. This represented a market share of mortgage stock of 2.0 per cent. Our growth of 16 per cent in mortgage balances during the year significantly exceeded market growth of 1.8 per cent. We increased our proportion of loans to first-time buyers during the year to 14 per cent of our gross residential mortgage lending. We also continue to support the Government's Help to Buy Guarantee and Equity Loan schemes and completed more than 4,000 of these loans during the year.

Our mortgage business remains high-quality and is comprised of 83 per cent residential and 17 per cent buy-to-let mortgages. The average loan-to-value of new mortgage lending was 68.0 per cent in 2015. Impairments in our mortgage business increased slightly during the course of the year as a result of portfolio growth. This was partially offset by strong arrears performance, with loans over three months in arrears at 0.22 per cent, significantly below the latest CML industry average of 1.12 per cent.

Buy-to-let continues to support the demand for private rented accommodation and our buy-to-let lending is high-quality. The average loan-to-value of stock was 55.4 per cent at 31 December 2015, and our affordability and rental cover requirements are among the most prudent in the sector. As such, we do not expect the new tax regulations for buy-to-let landlords, including the new additional 3 per cent stamp-duty announced in the Autumn Statement, to have a material impact on our business. We were delighted to win the 'Best Service from a Buy-to-Let Lender' award at the 2015 Business Moneyfacts Awards.

We have a thriving intermediary business and continued to invest in improving the service we provide to our Intermediary Partners. The launch of our refreshed intermediary proposition, which reinforces our commitment to offering excellent service to our Intermediary Partners, was well received and resulted in a significant improvement in our Intermediary Net Promoter Score (NPS), from +25 in 2014, to +40 in 2015. The quality of our intermediary service was recognised by winning the prestigious 'Best Lender for Partnership', at the Legal & General Mortgage Club Awards.

We are pleased with the ongoing strength of the mortgage business, having achieved a market share of gross mortgage lending of 3.4 per cent in 2015. We will continue to build on this strong foundation and target a market share of more than 3.0 per cent in the future.

Credit cards

During the year we made significant strides with our credit card business, including successfully migrating over 675,000 customer accounts from MBNA to our own platform. We developed the platform in partnership with leading systems provider TSYS which gives us full control of our credit card operation.

Improving consumer confidence in the UK has seen a general upward trend in demand for unsecured borrowing, and new business volumes since launching our new range of cards in April have been better than expected. Credit card balances increased to £1.6 billion at 31 December 2015, 44 per cent higher than at the end of 2014 and representing a 2.5 per cent share of the £65 billion market. Growing credit card balances will enable us to achieve a more efficient use of our capital.

The financial performance of the card business has been strong at both a new business and portfolio level. The overall contribution was £51.2 million at 31 December, 13 per cent higher than 2014.

The FCA published their interim findings from their market study into credit cards in November 2015, noting that competition is working fairly well for most consumers. The final report is expected to be published in spring 2016. If changes are required by the FCA, our platform and capability give us confidence that we will be able to comply with limited economic impact.

We are excited about the future of our credit card business. In 2014 we announced that we aimed to grow credit card balances to at least £3 billion by the end of 2018. We now aim to reach that target a year earlier by the end of 2017.

Deposits

The UK savings market has continued to grow strongly, helped by a positive economic backdrop and supportive government policy, including the increases to ISA limits and the introduction of the new Help to Buy ISA.

During 2015, our deposits franchise continued to flourish and our funding position is strong. Deposit balances grew by 12 per cent to £25.1 billion in 2015, a market share of 1.5 per cent. Deposit balances are now higher than at any point in our history.

We offer customers a range of competitively-priced instant access and fixed term savings products, both available as ISAs, through all our channels: store, online, digital, postal and telephone. Our online-led distribution model, supported by our efficient national store footprint, continues to be a key factor in growing our retail deposit business cost effectively. We continue to support customers' home ownership aspirations and as such we launched our Help to Buy ISA on 1 December 2015. The Help to Buy ISA is a way for first-time buyers to save tax efficiently and receive government assistance towards their first home deposit.

Access to wholesale funding to support growth

Our funding strategy is to access wholesale funding to supplement our core retail deposit base in order to optimise funding costs, extend tenor and ensure we have appropriate diversification in the funding base.

In April 2015, we issued £300 million of senior unsecured debt, our debut issuance under our Medium Term Note (MTN) programme. In addition, we have an established Residential Mortgage Backed Securities (RMBS) programme with a strong reputation, from which we raised a further £750 million in

Chief Executive's Review

June 2015. In January 2016, Gosforth 2016-1 raised a further £803 million of funding across three tranches denominated in Sterling, Euros and U.S. Dollars.

This was the first time a Gosforth RMBS had raised funding in U.S. Dollars, in addition to its presence in the Sterling and Euro markets, and we were delighted with the response from investors. We also accessed the Funding for Lending scheme to support lending growth and liquidity.

As we develop our wholesale funding programmes, our mix of wholesale may rise but will remain relatively low as a proportion of overall funding. We have amended our risk appetite to accommodate a loan-to-deposit ratio of up to 115 per cent, from 110 per cent, as a result of our successful participation in the wholesale markets. Our loan-to-deposit ratio was 107.5 per cent at 31 December 2015.

Increased wholesale funding and careful management of our retail deposit book reduced our weighted average cost of funds to 1.43 per cent in 2015 from 1.69 per cent in 2014.

Current Account, Insurance and Investments

The Virgin Essential Current Account (ECA) is now available across our network of 75 Stores, following the full national roll-out which completed in March 2015. Our potential to grow profitably at scale in current accounts is currently limited by the structure of the UK current account market, including the low level of switching and the predominance of free-if-in-credit banking.

We launched our new simple life insurance product in partnership with Friends Life in March and we continue to develop our general insurance proposition with Ageas to complement our successful travel insurance range.

We launched three new investment funds during the year, increasing the number of passively managed funds in our range to five. The new funds provide our customers with more choice and will support growth in our funds under management. Our funds under management stood at £3.0 billion at 31 December 2015, helping to drive a 9 per cent increase in investment income. The launch of these insurance and investment products creates the foundation from which to grow our non-interest income.

Maintaining a high-quality balance sheet

In 2015, we continued to manage our balance sheet within our prudent risk appetite with a view to maintaining its quality and efficiency. Our Common Equity Tier 1 ratio was 17.5 per cent at the end of 2015. Our total capital ratio was 20.2 per cent and our leverage ratio was 4.0 per cent at 31 December 2015.

Our liquidity position remains strong and we remain confident, though not complacent, that our liquidity policy enables us to achieve an appropriate balance between profitability and liquidity risk. In October 2015, the Liquidity Coverage Ratio (LCR) was introduced by the PRA as the Pillar 1 standard for liquidity in the UK.

Our LCR was significantly above the regulatory minimum at 202 per cent, reflecting our focus on ensuring high quality liquidity positions.

In November 2015, the rating agency Fitch revised Virgin Money plc's outlook to Positive from Stable and affirmed our long-term rating at BBB+. Fitch noted this reflected a well-managed low risk profile, which has resulted in healthy asset quality and improving profitability.

Strong financial performance

Our underlying return on tangible equity strengthened from 7.4 per cent to 10.9 per cent as a result of the successful delivery of our business plan for 2015. Key contributors to this improvement were strong growth in lending and an improvement in our net interest margin, enabling us to grow income during the year by 19 per cent. We continue to deliver on our cost efficiency targets. Underlying cost growth during the year was limited to 5 per cent, and we improved our cost:income ratio to 63.6 per cent in 2015 from 72.5 per cent in 2014. We will continue to take advantage of our operational leverage and drive efficiency in the business. We are well positioned to achieve a cost:income ratio of 50 per cent as planned in 2017.

Colleagues

We were delighted with the results from our Colleague Engagement Survey for 2015. The results indicate that our culture, underpinned by our ambition to make 'everyone better off' (EBO), our philosophy and approach have the full backing of our colleagues. Engagement scores compared strongly against industry standards at 88 per cent, with 92 per cent of colleagues fully supporting our values and 86 per cent believing strongly in Virgin Money's goals and objectives.

Our EBO culture sustains a virtuous circle based on a commitment to the communities in which we work and raises awareness of the Virgin Money brand and business as a force for good. Our culture cannot be readily and credibly replicated in the UK banking sector and it provides the foundation for our strategy and differentiated approach to banking.

Customers

We offer our customers straightforward products, supported by the delivery of outstanding customer service, through all forms of distribution channels including online, mobile, intermediary, store, telephone and also through our Virgin Money Lounges.

During the year our approach was rewarded and we now have over 3 million customers and a year-on-year improvement in customer satisfaction ratings. Our overall NPS, which is the measure of customer service and the likelihood of customers recommending us, improved in the year from +14 to +19, maintaining our position as one of the leading UK retail banks for customer service.

Investment in the digital channel in 2015 has continued to develop both functionality and content to enhance our customer experience. Customers are increasingly accessing our products and services online through mobile devices, with almost 40 per cent of website visits in 2015 made in this way, up from 29 per cent in 2014.

In August 2015, we opened our sixth Virgin Money Lounge in Haymarket, London. The Lounges delivered an NPS of +86 and are a strong commercial success. As a result, we will open a new customer Lounge in Sheffield in 2016.

Management team

To support continued growth in the business and the planned expansion of product lines, we have strengthened the Executive further. We are delighted that Peter Bole will be joining us as Chief Financial Officer in 2017, and Hugh Chater will join the business by June 2016, as Chief Commercial Officer. George Ashworth has joined the business as Managing Director, SME, to lead the development and strategy for Virgin Money in small and medium-sized enterprise (SME) banking.

Harnessing the talents of women in financial services

In July 2015, the government asked me to lead the review into the representation of women in senior managerial roles in the financial services industry. This followed concerns that, whilst equal numbers of men and women are entering the financial services sector, it appears that many women do not progress from middle to senior management. Businesses perform better when they include the best people from a range of backgrounds and many employers are already taking steps to increase diversity, including gender diversity.

My preliminary recommendations proposed that firms appoint an Executive responsible for gender diversity and report publicly on their progress. Also, organisations should link Executive bonuses to the appointment of senior women. Final findings are due to be published in March 2016.

Outlook

The macro environment has changed materially for banks like Virgin Money over the past 12 months. In particular, the year has seen the introduction of a new bank tax surcharge, the timetable for UK rate rises continues to be pushed back and we have seen regulatory concerns in the buy-to-let mortgage market. In addition, there are the emerging capital regulations from Europe. This has resulted in uncertainty relating to the potential for continued growth and profitability for banks of our scale in the sector. We think very carefully about our operating environment to ensure the business is able to continue delivering sustainable success for all stakeholders.

The tax rate for UK banks will rise by 8 percentage points to 28 per cent in 2016, as a result of the bank tax surcharge announced in the 2015 Summer Budget. We understand that in taking this action HM Treasury has started to level the playing field on the taxation of banks. Nevertheless, there is still much to be done to level the playing field overall. The CMA has a significant opportunity to intervene in the personal current account market, as part of their investigation into the current account and business banking sectors. This would open UK retail banking up to improved competition and it would go a long way to levelling the playing field in a way that would underpin strong competition and ensure that customers are better served in the future.

In 2015, we anticipated two increases to the official Bank Rate. However, interest rates remained at their historical low. Our results demonstrate that we have the flexibility to deliver on our targeted return levels, despite the lower for longer interest rate environment. As a result of the benign interest rate environment, which provides supportive credit conditions, and our highly robust underwriting standards, we expect our high asset quality to be maintained in 2016. When the Bank Rate does begin to rise, subsequent increases are expected to be gradual and limited.

In the mortgage market, the continuation of positive domestic economic factors and competitive mortgage deals all helped to underpin demand. We were able to take a strong share of the market, protect spreads and maintain asset quality. In addition, we also demonstrated our ability to grow our credit card book strongly. During the year, our weighted average cost of funds reduced against a background of falling deposit interest rates across the market, which broadly offset pressure on mortgage margins.

Chief Executive's Review

All of these things together, including signs of mortgage pricing stabilising in 2016, mean that we have confidence in growing assets at the right price, supported by high asset quality and low impairments, and funding that growth in a cost efficient way. This will support our earnings and therefore our capital position for the future.

Given our successful participation in the wholesale markets, we have amended our risk appetite to accommodate a loan-to-deposit ratio of up to 115 per cent. This will support our aim of increasing balance sheet efficiency and funding diversification.

We are very clear on the concerns raised by policymakers regarding the buy-to-let market. We are also very aware of the risks posed should the market become overheated, and the associated economic and political risks. The lack of housing supply in the UK supports the demand for private rented accommodation and a material number of people are going to want to rent for the foreseeable future.

We have built our participation in the buy-to-let market with that in mind. We focus on buy-to-let for retail customers, rather than portfolio landlords, and our affordability and rental cover requirements are among the most prudent in the sector.

We review our capital structure on an ongoing basis to ensure it is well placed to react to prevailing economic and regulatory conditions. We are delighted with our strong capital position and excellent asset quality, as the UK and European regulatory frameworks continue to evolve. As a result of the confidence we have in our strong capital position we believe that it is right, despite uncertainty in the macro environment, to pay a dividend. Given our capital position, even following the payment of dividends, our outlook for capital remains strong.

The UK will hold a referendum on its continued membership of the EU on 23 June 2016. The potential for Brexit will weigh on the prospects of the UK economy and there could be a lengthy period of elevated uncertainty should there be a vote in favour of an exit.

As a result of the strength of the business and our continued ability to manage our cost base, we are well placed to hit our targeted returns. We are able to absorb the impact of the new bank tax surcharge and are well placed to achieve a mid-teens return on tangible equity by the end of 2017.

In addition to our core business, we have new opportunities in SME, Personal Current Accounts (PCA) and unsecured lending to continue to grow. The SME market is underserved by the large incumbent banks and we continue to develop our strategy accordingly. We are also conducting a PCA feasibility study with a view to defining our entry into the broader PCA market.

To conclude, we are delighted that we have delivered strongly against our objectives in 2015. I would like to extend my thanks to our Virgin Money Colleagues for their hard work and achievements over the year, and to our customers, corporate partners and shareholders who play such an important part in our success. We will continue to put customers at the heart of everything we do and look to the future with confidence.

Jayne-Anne Gadhia CBE
Chief Executive
1 March 2016


Virgin Money Lounge, Haymarket, London

Market Overview

As a UK retail bank we are focused on serving domestic customers and continue to support and benefit from the UK economy and housing market.

UK economy

UK gross domestic product (GDP) increased by 0.5 per cent in the three months to the end of December, taking the annual rate of growth for 2015 to 2.2 per cent. This was an improvement on the third quarter of 0.4 per cent but the annual growth was down compared with 2.9 per cent in 2014. GDP is the main indicator of economic growth and, despite the annual pace of growth being the slowest for three years, it still means the UK is amongst the fastest growing developed nations.

We remain alert to the downside risks related to the impending UK referendum on EU membership, the recent market volatility caused by weakness in the global economy, and the uncertain outlook for interest rates.

The UK will hold a referendum on its continued membership of the EU on 23 June 2016. The referendum is likely to cause a degree of business uncertainty and result in a dampening impact, as the potential for Brexit weighs on the prospects of the UK economy. In addition, global growth is coming under pressure, primarily due to a slowdown in emerging markets and falling commodity prices. This, combined with political tension in the Middle East, also has the potential to impact adversely the UK economy.

For 2015 as a whole, consumer price inflation averaged zero per cent, its lowest level since comparable records began in 1950. Weakening inflationary pressures, as a result of lower costs for energy and food and weakness in emerging markets, are likely to keep consumer price inflation below 1 per cent until the second half of 2016, which should provide a net stimulus to businesses and households and therefore the UK economy. The Bank of England kept the official Bank Rate at 0.5 per cent in 2015, noting that a slowdown in emerging markets could exert a bigger drag on UK growth and inflation. When the Bank Rate does begin to rise, subsequent increases are expected to be gradual and limited. As a result, mortgage and credit card arrears are expected to remain low.

Based on the HM Treasury consensus view, which we use and consider in our strategic planning, we believe the most likely outlook is slightly slower GDP growth in 2016, compared to 2015. The current consensus for 2016 GDP growth is 2.1 per cent.

Global equity markets had a difficult start to 2016, as a result of rising concerns over slowing economic growth in China and falling commodity prices. According to the International Monetary Fund's latest forecast, growth in China is expected to slow to 6.3 percent in 2016 and 6.0 per cent in 2017, primarily reflecting weaker investment growth as the economy continues to rebalance.

Housing and Mortgages

Housing activity ended 2015 stronger than it started. The continuation of positive domestic economic factors and competitive mortgage deals, helped to underpin household demand, but housing transaction volumes still remain notably weaker than pre-crisis levels. Growth in UK house prices continued in 2015, as a result of improving economic conditions and household finances, together with sustained low mortgage rates boosting housing demand. Demand for housing continues to outstrip supply, maintaining upward pressure on house prices. This pressure on house prices is likely to continue given the lack of housing supply and limited number of properties on the market. Housing starts and completions in the 12 months to September 2015 in England totalled just over 135,000, a figure which remains about 25 per cent below pre-crisis peaks. The ongoing shortage of housing supply continues to be a constraint on housing market activity.

The Bank of England said in January 2016 that the UK's economic recovery has not been debt-fuelled, and pointed to aggregate private credit growth being modest compared to pre-crisis conditions. Increased focus is being given to areas of more buoyant activity such as buy-to-let mortgages, unsecured consumer credit and the still-elevated levels of household debt relative to income. This may result in macro-prudential action where appropriate, given the possibility of a prolonged period of relatively low interest rates encouraging the build up of excessive risks.

As announced in the Autumn Statement, people purchasing buy-to-let properties and second homes will pay an extra 3 per cent in stamp duty from April 2016. In December 2015, the Bank of England reiterated concerns about activity in the sector, and HM Treasury published a consultation on powers of direction for the Financial Policy Committee (FPC) in the buy-to-let market. We are clear on the concerns raised by policymakers, and the effect new measures may have on the size of the market. We focus on buy-to-let for retail customers, not portfolio landlords, and our affordability and rental cover requirements remain very prudent. As a result, we do not expect these changes to have a material impact on our business.

Savings

Robust growth in disposable income and consumers' reduced sense of caution, reflected in a historically low savings ratio, supports the outlook for consumer spending. Despite this, the outlook for the retail savings market continues to be strong. There are a number of macro-economic factors supporting this positive growth outlook, including low inflation rates driving real returns on cash savings and rising rates of real wage growth, increasing the capability to save. In addition, government policy, including increased ISA limits, the new personal savings allowance and reduced pension tax relief should increase the relative attractiveness of cash savings.

From a regulatory perspective, the FCA published its cash savings market study report in January 2015, and published new measures for cash savings accounts to boost competition in December 2015. The remedies are designed to improve disclosure, switching and convenience for customers in the retail savings market. From December 2016, firms have to provide clear information on interest rates offered on cash savings products as well as clearly reminding consumers about changes in interest rates or the end of an introductory rate. We agreed with the conclusions of the FCA study and continually strive to offer good value products to all of our savings customers.

The reduction in the Financial Services Compensation Scheme (FSCS) protection limit from £85,000 to £75,000, announced in July 2015 and taking effect from 1 January 2016, is expected to lead to an increased level of customer activity as consumers move their savings to ensure they remain within the new limits.

Credit Cards

The FCA published their interim findings from their market study into credit cards in November 2015, noting that competition is working fairly well for most consumers. According to the FCA, there are currently about 30 million credit cardholders in the UK, with an estimated £65 billion of outstanding credit card balances – or an average of £2,000 per person. Consumers value the flexibility offered by credit cards and attractive introductory promotional offers are a common feature. We agreed with the FCA's interim findings and the proposed requirements for full transparency and responsible lending. We also welcomed the FCA's support for a range of products, including zero per cent balance transfer products, which are so popular with UK consumers. The final report is expected to be published in spring 2016. If changes are required by the FCA, our platform and capability give us confidence that we will be able to comply with limited economic impact.

Personal Current Accounts (PCA)

In October 2015, the CMA published its provisional findings as part of an in-depth investigation into the £16 billion current account and business banking sectors. The CMA found that banks do not have to work hard enough to compete for customers and identified a number of competition problems in both the PCA and SME banking markets. They found that low levels of customer switching mean that banks are not put under enough competitive pressure, and new products and new banks do not attract customers quickly enough. As such, the report proposed a better deal for bank customers and proposed remedies which focused heavily on switching, transparency and comparability. We welcomed the report from the CMA but considered its provisional findings did not go nearly far enough to tackle the closed shop of the large incumbent banks and transform such an important market. Intervention is required to open the UK retail banking market up to the full force of true competition and ensure that customers are better served in the future. We will continue to engage with the CMA ahead of the publication of its final report.

Regulation

Capital developments – CRD IV

CRD IV introduced new capital limits and buffers for banks, and includes a requirement to hold Common Equity Tier 1 capital to account for capital conservation, countercyclical and systemic risk buffers. We review our capital structure on an ongoing basis to ensure it is well placed to react to prevailing economic and regulatory conditions. Our Common Equity Tier 1 capital ratio was 17.5 per cent as at 31 December 2015, compared with a fully loaded regulatory minimum of 7.0 per cent, comprised of Common Equity Tier 1 capital of 4.5 per cent and a capital conservation buffer of 2.5 per cent.

CRD IV also introduced a new leverage ratio requirement. The leverage ratio is a non-risk based measure that is designed to act as a supplement to risk based capital requirements. It is intended as a back stop measure. The leverage calculation determines a ratio based on the relationship between Tier 1 capital and total consolidated exposure. Our leverage ratio was 4.0 per cent at the end of December 2015. There is no minimum requirement until we exceed deposit balances of £50 billion. At present we maintain a prudent risk appetite for leverage.

Market Overview

Ring-Fencing
Ring-fencing is scheduled to be implemented fully into the UK banking system by 1 January 2019. It is expected that Virgin Money will operate as a wholly ring-fenced bank, and both transitioning and managing in accordance with the proposed requirements will be less onerous than is the case for many larger and more complex entities.

Minimum Requirement for Eligible Liabilities (MREL)
Minimum Requirement for Eligible Liabilities (MREL) is applicable from 1 January 2016, and will be phased in fully by 1 January 2020. Prior to 31 December 2019, MREL will be equal to an institution's minimum regulatory capital requirement. Virgin Money expects the Bank of England to provide a prospective MREL during 2016, with transitional arrangements to 1 January 2020.

Payment Systems Regulator (PSR)
The new Payment Systems Regulator launched on 1 April 2015 with an objective to promote competition and innovation and to ensure payments systems are operated and developed in the interests of the people and businesses using them. We have been very supportive of the establishment of a new Payment Systems Regulator and view access to payment systems as a key issue holding back competition in UK retail banking, especially in the PCA market. It is essential that the UK payments system is open, transparent and easy to access. This will drive increased competition which will benefit everyone who uses payment systems.

EU Mortgage Credit Directive (MCD)
We will implement the MCD requirements by 21 March 2016. The MCD provides an EU-wide framework of conduct rules for mortgage activities. It sets minimum regulatory requirements that member states must meet to provide consistency in protecting consumers taking out credit agreements for residential property.

Competitive drivers

Virgin Money benefits from being a simple and straightforward retail bank unburdened by legacy issues. As one of the foremost consumer champion brands in the UK, we are also focused on ensuring good outcomes for all of our customers as their expectations and demands continue to rise.

In the current low interest rate environment, many customers are motivated by their desire to achieve better value for money, but security and reputation remain important factors.

We believe customers want straightforward and transparent products combined with the ability to access their products and services through the channel of their choice. Service remains one of the key drivers of customer satisfaction and customers are increasingly less forgiving of poor service.

Demand for multi-channel banking is established and customers expect to be able to manage their finances whenever and wherever is most suitable for them, whether by telephone, online, or by using their mobile device.

Market trends

Key opportunities:

- economic environment: strongly capitalised and well positioned to continue growing in the context of the resilient UK economy and housing market;
- customer needs: our differentiated and customer-focused strategy along with multi-channel customer access, in particular our developing digital capability, mean we are well positioned to address evolving customer needs; and
- regulatory environment: increasing clarity on regulatory requirements and our uncomplicated, low risk business model, unburdened by legacy, place us in a strong position.

Key challenges:

- macro environment: economic uncertainty as a result of the potential for Brexit and the weakness in the global economy, with the potential knock-on effect to the UK economy;
- buy-to-let: a number of tax measures will be implemented in 2016, and these may have a dampening effect on future growth prospects for buy-to-let and the private rented sector; and
- digital transformation: the pace of change continues to be significant and we will need to continue to invest to meet evolving customer needs.

Virgin Money Lounge, Haymarket, London

Business Model and Strategy

Company

At the heart of everything we do is our ambition to make everyone better off.

Our business model

Virgin Money is a strong, low risk retail-only bank which is focused primarily on providing residential mortgages, savings and credit cards. We offer a range of investment and insurance products and the full national roll-out of the Virgin Essential Current Account (ECA), a market leading Basic Bank Account, was completed in March 2015.

We provide award-winning customer service to over 3 million customers through a range of channels, including online and mobile, intermediaries, call centres and a national network of 75 Stores and six customer Lounges. Our business model positions us well for cost-effective growth in an increasingly digital world. By leveraging our strategic assets and capabilities, we remain focused on creating a business with a demonstrable track record of growth, a balance sheet of the highest quality, and delivering a history of strong shareholder returns.

Our vision

Our aim is to make ‘everyone better off’ by delivering good value to our customers, treating colleagues well, making a positive contribution to society, building positive relationships with our partners and delivering sustainable profits to our shareholders. The ambition to make ‘everyone better off’ continues to underpin Virgin Money’s differentiated approach to banking.

Our distinctiveness

The foundations for providing a distinctive customer proposition are: our powerful brand, our customer-focused culture, our financial strength and our legacy-free approach. Our ambition to make ‘everyone better off’ runs through our culture and decision making, and is key to ensuring we are building a sustainable model for all our stakeholders, and living up to the trust they place in us.

How we create value

A low risk, customer-focused UK banking model, delivering straightforward, transparent products that treat customers fairly.

GROWTH

Through straightforward, transparent products

> gross mortgage lending at 3.0% or better;

> credit card balances to at least £3.0 billion by the end of 2017.

QUALITY

Through our customer focused culture

> asset quality maintained.

> at a minimum:

- 12.0% Common Equity Tier 1 ratio;
- 15.0% total capital ratio.

RETURNS

Through financial strength

> return on tangible equity to mid-teens by the end of 2017;

> cost:income ratio of 50% by 2017.

Everyone’s better off

The Virgin Money business model and strategy is underpinned by our ambition to build a bank that makes everyone better off

Our competitive strengths

We are well placed to provide effective competition to the large incumbent banks in the UK across a number of markets. We have the potential for significant organic growth at meaningful scale across a broad range of products and are unburdened by legacy issues from the past. Our strategy is underpinned by Virgin Money's core business strengths:

> a high-quality balance sheet, set within a strong risk management framework, unburdened by legacy issues;

> a differentiated approach to banking and a brand that provides mass consumer appeal;

> a capacity for organic growth at meaningful scale;

> a significant potential to improve returns through operational leverage and positive margin development;

> a strong management team with a track record of delivering organic and inorganic growth, supported by highly engaged colleagues; and

> a strong culture that cannot be readily, and credibly, replicated provides the foundation for our strategy and differentiated approach to banking.

Our strategy for success

Our strategy is focused on growing strongly, maintaining a high-quality balance sheet and delivering attractive shareholder returns, whilst serving our other stakeholder groups – customers, colleagues, corporate partners and the communities in which we work.

OUR STRATEGY FOR SUCCESS

GROWTH
Page 24

QUALITY
Page 25

RETURNS
Page 26

EBO
Page 27

Delivering our Strategy: Growth

Building on our demonstrable track record of growth

Aim

We plan to continue to deliver strong growth across our core mortgages, savings and credit card businesses and enhance our activities in insurance and investments. We will also develop our SME strategy, define our entry into the broader PCA market and build our digital capability, to support continued growth in the business.

Progress in 2015

> our mortgage balances grew 16% to £25.5 billion, compared with market growth of 1.8%;

> we delivered gross mortgage lending of £7.5 billion, 29% higher than in 2014, giving a full year market share of 3.4%;

> our net mortgage lending performance of £3.6 billion in 2015 gave us a market share of 10.6%;

> our deposit balances grew 12% to £25.1 billion, the highest in Virgin Money's history, a market share of 1.5%; and

> we grew credit card balances to £1.6 billion at the end of 2015 compared to £1.1 billion at the end of 2014, giving a full year market share of 2.5%.

Priorities for 2016

> maintain annual gross mortgage market share of over 3.0%;

> continue to grow credit card balances towards at least £3.0 billion by the end of 2017;

> explore opportunities to grow our non-interest income by offering appropriate products and services to our existing customer base, leveraging our strong customer relationships and brand;

> develop the strategy for Virgin Money in SME banking;

> complete a PCA feasibility study addressing the barriers to profitable growth in the current account market, with a view to defining our entry into the broader market; and

> enhance our digital capability to support our growth ambitions.

Our approach to 2016

We plan to continue to achieve a market share of annual gross mortgage lending of over 3.0% and we are focused on delivering growth in key market segments. We will aim to increase lending to first time buyers, grow our new build proposition and target non-portfolio landlords in the buy-to-let market, within our prudent risk appetite.

We will continue to build upon our proven deposit gathering capability, attracting funds from both new and existing customers with straightforward and transparent products. We will continue to manage our cost of funds effectively and build on our proven ability to attract sticky deposits and our success in growing Cash ISA balances to over £10 billion.

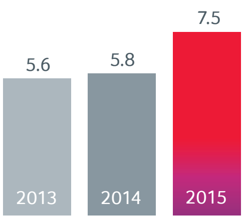
We will continue to grow our credit card business, as we seek to grow our cards book from £1.6 billion to at least £3.0 billion by the end of 2017. Growing credit card balances will enable us to achieve a more efficient use of our capital.

We will drive growth in our funds under management and start to grow our insurance business through our new range of products launched in 2015. Growing our investment and insurance businesses will increase the contribution of our non-interest income over time.

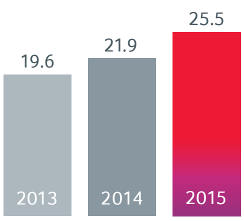
We continue to develop the strategy for Virgin Money in SME banking. The market is underserved by the large incumbent banks. As a result, the development of SME banking has significant potential to support growth in the business.

We have commenced a PCA feasibility study with a view to defining our entry into the broader PCA market.

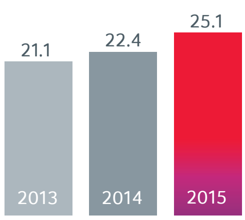
The digital transformation of UK retail banking is a focus for the business and we will continually adapt to the changing landscape of the future.



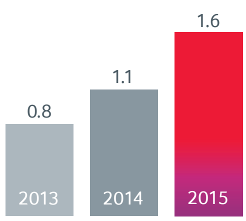
Gross Mortgage Lending (£bn)



Mortgage Balances (£bn)



Deposit Balances (£bn)



Credit Card Balances (£bn)

Delivering our Strategy: Quality

Maintaining a high quality balance sheet

Aim

We will maintain our focus on building a high-quality balance sheet, underpinned by robust asset quality and a prudent risk appetite.

Progress in 2015

- our Common Equity Tier 1 ratio was 17.5% at the end of 2015, compared with 19.0% at the end of 2014, as we continue to optimise our balance sheet within our prudent risk appetite;
- our leverage ratio was 4.0% at the end of 2015, a level we believe to be safe, conservative and supportive of our growth plans;
- our mortgage arrears remained low, with loans over three months in arrears at 0.22%, compared with the latest CML industry average of 1.12%;
- our loan-to-deposit ratio increased to 107.5% from 102.8%, in line with our aims of increasing balance sheet efficiency and funding diversification;
- our credit card arrears remain below industry average, with 0.96% of balances two or more payments in arrears in 2015, compared with 1.46% in 2014; and
- our cost of risk at 0.12% in 2015 reflects our high-quality asset base and was driven by our conservative risk appetite and rigorous credit decisioning.

Priorities in 2016

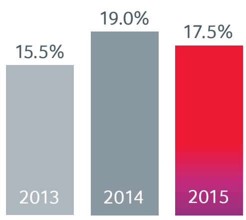
- maintain strong capital ratios, with a minimum 12.0% Common Equity Tier 1 ratio; and
- maintain current asset quality and a low cost of risk through a robust risk management approach.

Our approach in 2016

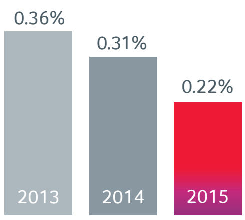
Our focus on maintaining a high-quality balance sheet is supported by our conservative risk appetite and our robust approach to risk management.

Our defined risk appetite imposes tight controls on a range of criteria including, for mortgages, loan-to-value ratios and business mix and, for credit cards, application scores. As a result of the rigorous application of this approach, Virgin Money's credit quality is significantly better than the industry average in mortgages and credit cards.

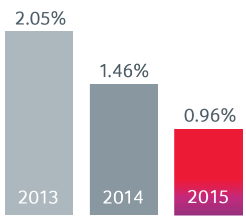
We will continue to increase our balance sheet efficiency and funding diversification as we continue to fund our targeted scale of asset growth. As a result we have increased the upper limit of our loan-to-deposit ratio to 115% over time, from 110%.



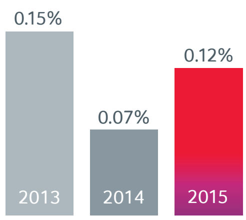
CET1 Ratio



Mortgage Arrears



Credit Card Arrears



Cost of Risk

Delivering our Strategy: Returns

Delivering a strong financial performance

Aim

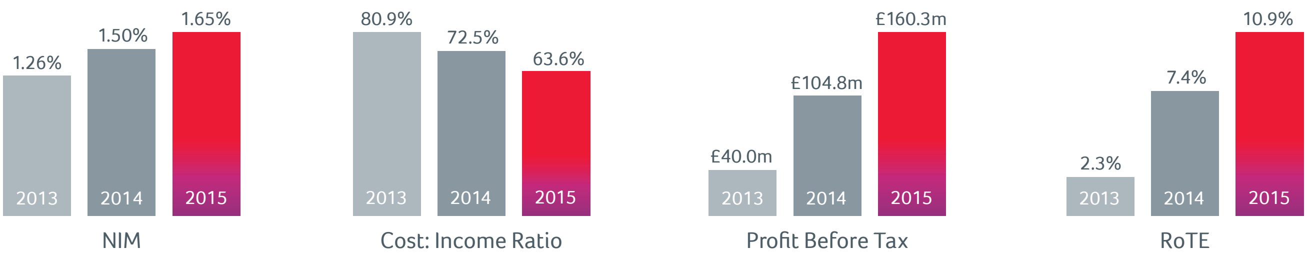
We target a mid-teens return on tangible equity by the end of 2017.

Progress in 2015

- we delivered continued improvement in returns during the year, in part reflecting asset growth from £26.5 billion at the end of 2014 to £30.2 billion at the end of 2015;
- our underlying net interest margin was 1.65% during 2015, up from 1.50% during 2014, driven by optimisation of the mortgage business and a reduction in our weighted average cost of funds to 1.43%;
- net interest margin improvements, added to our asset growth, meant that we delivered underlying total income growth of 19% in 2015, compared with underlying expenses growth of 5%;
- our underlying profit before tax increased 53% to £160.3 million in 2015, from £104.8 million in 2014;
- our underlying return on tangible equity increased to 10.9% in 2015 from 7.4% in 2014; and
- our statutory profit before tax of £138.0 million for 2015 compared to a statutory profit before tax of £34.0 million in 2014.

Priorities for 2016

- continue to build upon our strong track record of income growth;
- maintain our focus on cost management, which aims for a cost:income ratio of 50% by 2017. We will exploit our operational leverage to maintain the positive differential between income and cost growth in the years to come;
- continue to maximise our net interest margin within our prudent risk appetite; and
- explore opportunities to grow our non-interest income by offering appropriate products and services to our existing customer base, leveraging our strong customer relationships and brand.



Delivering our Strategy: Everyone's better off

Our path to sustainable competitive advantage

Our ambition is to make 'everyone better off'

In 2015, we have delivered strongly to all of our stakeholders, living up to our ambition to make 'everyone better off'. The ambition to make 'everyone better off' sits at the heart of our business and underpins the way we go about doing business today, as well as the approach we are taking to creating products and services for the future. We believe that by building a bank that aims to make 'everyone better off', we can deliver strong, sustainable returns to our shareholders.

EBO is a virtuous circle

EBO helps build customer trust by informing our principles in straightforward and transparent product design, providing both new and existing customers with good value products and delivering excellent service. This approach enhances customer recruitment, satisfaction and retention performance. This has real economic benefits to the business. Our cost of acquisition is reduced and it encourages both personal recommendation from our customers and multi-product holding.

EBO also helps us to recruit and retain excellent colleagues. It creates the right environment for all colleagues to develop and flourish and, importantly, engages our people beyond financial reward, as our engagement scores indicate.

An important part of Virgin Money's business model and strategy is our contribution to the communities in which we work. Virgin Money Giving is Virgin Money's not-for-profit fundraising website, which makes it easy for people to donate money online to charities of their choice. Since its launch, more than £420 million has been raised for charities through Virgin Money Giving.

The partnership with the Virgin Money London Marathon has made an important contribution to this growth. Virgin Money Giving and the London Marathon both help to raise awareness of the Virgin Money brand and business as a force for good.

In 2015, Virgin Money launched the Virgin Money Foundation (the 'Foundation') – a new, independent charitable foundation that will focus initially on community projects in the North East of England, and over time will grow to operate nationally. The Foundation will promote the sustainable regeneration of economically and socially deprived communities in the UK.

Our EBO philosophy creates real confidence and trust amongst our corporate partners. Knowing they are working with or investing in a business with EBO at its heart, focused on mutually beneficial outcomes, ensures business goals and plans are fully aligned. By delivering to our other stakeholders, we reinforce our ability to deliver to our Company and shareholders.

EBO is unique to Virgin Money

The culture that sustains our ambition to make 'everyone better off' cannot be readily, and credibly, replicated in the UK banking sector and it provides the foundation for Virgin Money's strategy and differentiated approach to banking.

Delivering to our Stakeholders

Customers

At Virgin Money, we have a strong, customer-focused culture. In 2015 our philosophy was rewarded with growth in new customers and customer satisfaction, as well as improved retention.

Aim

Our aim is to be positively different from the incumbent banks by offering straightforward products with fair and transparent pricing, supported by the delivery of outstanding customer service, through the channels our customers prefer to use.

Achievements in 2015

> attracted over 640,000 new customers since the start of 2015, due to strong performance across our core Mortgages, Savings and Credit Card products;

> improved customer satisfaction and advocacy with an increase to +19 in our overall net promoter score (NPS), and resolved 100%[1] of complaints within eight weeks;

> opened a new Lounge in Haymarket, London in August 2015. The NPS for our award-winning Lounges was +86;

> completed the national rollout of our market-leading Basic Bank Account, the Virgin Essential Current Account; and

> launched new, straightforward and easy to use products to customers across our insurance and investment business, as well as our new Travel Money & International Money Transfer services.

1 Excluding speculative PPI complaints.

Priorities for 2016

> continue to invest in building our customer service capability;

> maintain a culture where customer service is a priority;

> deliver market-leading customer satisfaction;

> continue to provide straightforward, transparent products that treat customers fairly;

> enable customers to access our products and services wherever they are and through the channel they prefer; and

> continue to grow the Lounge network.

Performance in 2015

Net Promoter Score (NPS)

Customers

Virgin Money operates a digitally-led distribution model supported by Stores, Lounges and Contact Centres. Virgin Money's website remains the most popular channel for customers, with 76% of Virgin Money's sales carried out digitally, and over 17.3 million website visits during 2015.

Digital capability

We continued to improve our digital capability to make it easier for our customers to access Virgin Money services and products using their mobile devices. As a result we now have more than 2.2 million customers using our digital services, including 680,000 customers who accessed services from a mobile device.

In December 2015, we commenced a Colleague pilot of Smartr, a mobile app that has been designed to help our customers get more from their spending money. Smartr learns what a customer likes to spend their money on and personalises offers accordingly.

The digital transformation of UK retail banking is a focus for the business. We will continually adapt to the changing landscape of the future to ensure we enhance our customer service and experience accordingly.

Lounges

The Virgin Money Lounges won the Customer Experience of the Year Award for Banking in the UK Customer Experience Awards. These awards recognise companies who deliver an outstanding customer experience in their field. The Lounges also won the inaugural UK Financial Services Experience Awards for innovation in 2015. See more on our Lounges concept in the case study on page 30.

Financial inclusion

Virgin Essential Current Account

As part of our ambition to make 'everyone better off' we launched The Virgin Essential Current Account (ECA), which we rolled out nationally during 2015. The ECA supports financial inclusion by setting a new standard for Basic Bank Accounts in the UK with no unpaid item fees and a fair rate of credit interest. It is a free basic bank account designed to help our customers stay in control of their money. It has all the main features of a current account including the ability to deposit and withdraw money through any UK Post Office but no overdraft facility, as required by the Basic Bank Account agreement. In November 2015, we updated our policy to accept applications from undischarged bankrupts to ensure that the account is available to everyone.

Virgin Money Lounge, Haymarket, London

TREATING YOU AS A PERSON, NOT A NUMBER

Our Lounges are about more than money and banking. They are designed to be places where our customers can relax and local communities come together. They are all part of our ambition to be a very different kind of bank – one that makes everyone better off.

Virgin Money Lounges are unique in UK banking.

Lounge visitors can choose to put their feet up and enjoy the facilities, use the Lounge for an informal meeting… and if a customer decides they want to undertake some personal banking, that choice is available too.

Access to Lounges is available for all Virgin Money customers, and membership is free. As part of Virgin Money's ambition to make 'everyone better off', Lounges are also available on request for use by the local community for events, charity meetings and fundraising activities.

The Virgin Money Lounges won the Customer Experience of the Year Award for Banking in the UK Customer Experience Awards. The UK Customer Experience Awards recognise companies who deliver an outstanding customer experience in their field. The Lounges also won the inaugural UK Financial Services Experience Awards for innovation in 2015.

The Lounges create valuable opportunities for both customer retention and recommendation. There have been over one million visits to the Virgin Money lounges since they launched in 2011.

We opened a new Lounge in Haymarket, London in 2015. Just a short walk from Piccadilly Circus, the new Haymarket Lounge takes the Virgin Money customer experience to a whole new level. The entrance level offers customers the chance to 'lounge', watch TV, or browse through a range of Virgin Money information on a huge interactive touch screen display. It also offers full banking facilities to customers in a strikingly designed banking area, with a beautiful virtual fish tank, complete with virtual Richard Branson diver!

When customers descend to lower ground, they may forget they're in a bank altogether and expect to be asked to take their seats for take-off. Given Virgin's history in aviation, the lower floor has been designed in the style of the interior of an airliner with real airliner seats, overhead lockers and floor lighting to guide the way. The generously-spaced seats can be arranged in cinema style to face a big screen, or easily swivelled to face each other for informal meetings. The aircraft theme extends to a children's playroom, which is equipped with a range of traditional and interactive games to keep the young ones entertained.

The new Haymarket Lounge is the sixth to be opened in the UK, following the Lounges in Edinburgh, London, Manchester, Norwich and Glasgow. All Virgin Money Lounges offer free refreshments and snacks, use of iPads, free wi-fi access, televisions to catch up on the latest news, daily newspapers and facilities to help keep children entertained.

The Lounges are a strong commercial success, driving higher customer acquisition, retention and multi-product holdings, and delivered an NPS of +86. Virgin Money Stores co-located with a Lounge outperform the network based on sales performance. As a result, we will continue to invest in the Lounge concept and will open a new Lounge in Sheffield in 2016.

"This place is amazing! The staff are wonderful! This is a fantastic idea. I am going to open an account after I leave here. I work with vulnerable people who often have no money and food, never mind a cup of tea, so to bring them here is an amazing treat for them. It is such a great idea. It really endears me to Virgin Money and I would consider a Virgin product over another with the same rates because of your generosity."

NPS **+86**

Kevin Lloyd Design@klloyddesign
Thank you @VMLounges Manchester for the lovely birthday surprise you gave our 3yr old daughter today. So very kind of you #manchester

DL@mcdaveyboy
@VMLounges 1st visit to the Edinburgh lounge today, friendly staff & lovely atmosphere. If only all companies treated customers like this

Delivering to our Stakeholders

Virgin Money Lounge, Glasgow

Colleagues

Virgin Money's success is built firmly on the commitment, skill and attitudes of all our people and our shared purpose of building a better bank which will make 'everyone better off'.

Aim

Our aim is to nurture a skilled, diverse and committed workforce where every individual – regardless of background – can share our purpose, reach their potential and be rewarded appropriately for their contribution to our success.

Achievements in 2015

Investing in colleague skills:

- continued investment in the development of all colleagues;
- implementation of focused line manager development; and
- establishment of a leadership programme for our leaders of the future.

Building colleague commitment:

- improved colleague engagement from 86% in 2014 to 88% in 2015 – a leading industry score;
- enhanced our performance management capability and its link to remuneration outcomes; and
- increased colleague share ownership to over 70%.

Creating a diverse workforce:

- appointment of Michele Greene, Strategic Development Director, to lead our diversity agenda from the heart of our Executive Committee;
- conducted a first analysis of gender pay gap issues;
- re-accredited as a 'two tick', 'Positive about Disability' employer, interviewing disabled candidates where minimum requirements for the role were met; and
- adopted 'blind' recruitment for all new roles.

Priorities for 2016

Investing in colleague skills:

- focus on line manager development to create a supportive workplace environment;
- execute on our 'Brilliant!' leadership programme to develop our Executives and create internal succession capability; and
- develop capability and technology to support an increase in flexible working.

Building colleague commitment:

- equip our leadership team with all they need to support and develop our culture and our colleagues;
- provide everyone with the tools, resources and training they need to excel in their role; and
- help everyone understand how their pay and performance is determined.

Creating a diverse workforce:

- begin the journey towards a gender balanced workforce of 50:50 by 2020;
- create an environment and culture which equally engages people of all backgrounds; and
- develop our capability to support the recruitment, training and career progression of disabled colleagues.

Diversity and Inclusion

During 2015, we made diversity and inclusion a strategic priority. Analysis shows that a diverse workforce produces superior results and greater customer alignment. We aim to create an organisation whose people properly represent the rich and broad nature of the UK population. We also aim to reward, develop and value every person equally for their contribution to our purpose and our business success.

In 2015 we analysed progress against our diversity and inclusion agenda and found we had some material actions to take in order to achieve our strategic objectives.

Notwithstanding our commitment to making progress across the broad diversity agenda, it is our intention in 2016 to focus on gender equality with a view to ensuring:

- that we achieve 50:50 gender balance (within a 10% tolerance) in each key employee category by 2020;

Our current gender breakdown is as follows:

	Gender	2015 Number	2015 %	2014 %
Board	Male	5	56%	70%
	Female	4	44%	30%
Senior management	Male	115	82%	77%
	Female	25	18%	23%
All colleagues	Male	1,373	44%	45%
	Female	1,726	56%	55%

Delivering to our Stakeholders

Colleagues

> that there is no statistically significant pay gap in any employment category by the time we meet our 50:50 target.

Details of our current gender pay gap are as follows:

Level	Reward Group	Headcount | %		Gender Pay Gap[1]
		Male	Female	
Executive	Exec 1	11 | 73%	4 | 27%	(29)%
	Exec 2	30 | 83%	6 | 17%	22%
Management	Band A	74 | 82%	16 | 18%	6%
	Band B	202 | 60%	136 | 40%	11%
Non-Management	Band C	205 | 65%	110 | 35%	4%
	Band D	557 | 48%	603 | 52%	2%
	Band E	294 | 26%	851 | 74%	(1)%

1 The difference between average male and female salary as a % of average male salary, based on FTE salary only.

Our reward and benefits structure is designed to be fair and free from discrimination. Whilst there are no equal pay issues for comparable roles, the table above highlights the need to redress the senior gender imbalance through enhancing our recruitment, development and pay practices.

In order to plan for the successful achievement of these objectives we have adopted the following approach:

> appointed a senior member of our Executive Committee to lead the programme (which is sponsored by the Chief Executive);

> implemented line manager training to align behaviours with our strategy;

> committed to reviewing our culture to make it more flexible, inclusive and balanced; and

> planned to provide technology and other support to facilitate flexible working.

It should be noted that this strategy is about gender equality. All of our policies apply equally to the brilliant women and men who provide such committed service to Virgin Money today.

We look forward to reporting our progress publicly against this important agenda.


Virgin Money Lounge Host, Norwich

Delivering to our Stakeholders

Corporate Partners

We look to partner with businesses that genuinely understand and share our philosophy of making 'everyone better off'.

Aim

We aim to maintain our strong track record in managing mutually beneficial relationships with corporate partners in order to complement our own business and core banking capabilities with our partners' technical product expertise and infrastructure.

Achievements in 2015

- worked with over 12,500 Mortgage Intermediary Partners and held over 100,000 meetings with them to support growth in our mortgage business in 2015;
- won the "Best Lender for Partnership with Mortgage Club" at the L&G Mortgage Club annual awards;
- partnered with TSYS to launch our own credit card business;
- launched three new investments funds, creating more choice for customers, working with our partners State Street Global Advisors and IFDS;
- implemented key changes required by the Government's Pension Flexibility Rules, with our partner IFDS;
- launched our new life insurance products through our partnership with Friends Life (now part of the Aviva Group) and new general insurance products through our partnership with Ageas; and
- launched our Travel Money proposition through our partnership with Travelex and our International Money Transfer proposition through our partnership with World First.

Priorities for 2016

- continue to innovate and deliver outstanding levels of service to our network of professional mortgage intermediary partners as we seek to become the lender of choice for intermediaries;
- continue to strengthen relationships with, and oversight of, our corporate partners;
- continue to build and strengthen our customer propositions through all of our corporate partnerships to support growth in our non-interest income; and
- enhance our customer communication strategy through our print and communications partner, Communisis, with a focus on enhancing our digital communication capabilities.

"Our relationship with Virgin Money has deepened over the last couple of years through an excellent process of engagement and a focus on delivering a proposition that meets the needs of brokers. This resulted in Virgin Money receiving the 'Best Lender for Partnership' Award at our Mortgage Club Awards last year and we very much look forward to continuing to develop our business relationship and look forward to another strong year in 2016."

Stephen Smith
Director, Housing Partnerships
Legal & General

"We are delighted to be working together with Virgin Money to support their customers. Virgin Money is well known for its outstanding level of customer service and highest quality products and we are proud to be its trusted partner to deliver its insurance proposition."

Ant Middle
Chief Executive Officer
Ageas Retail

Corporate Partners

Mortgage Intermediary Partners

Our Intermediary Partnerships remain a key part of the Virgin Money mortgage strategy. During 2015, we maintained our strong reputation for customer service and continued to invest in improving the service we provide to our intermediary partners as we seek to become the lender of choice for intermediaries.

We had a very positive reaction to the launch of our refreshed intermediary proposition in February 2015. The commitments we made to our Intermediary Partners reflect the value we place on this channel. Intermediaries have become increasingly important to both mortgage customers and providers since the introduction of the Mortgage Market Review and our key focus and competence in this channel gives us confidence in continued growth.

As part of our service commitment, we wrote to our Intermediary Partners to introduce and summarise the key changes relating to the EU Mortgage Credit Directive (MCD), to help them prepare for the implementation date of 21 March 2016. The MCD provides an EU-wide framework of conduct rules for mortgage activities.

Our success in supporting our Intermediary Partners during 2015 was recognised by winning the 'Best Service from a Buy-to-Let Lender' award at the Business Moneyfacts Awards, as well as the prestigious 'Best Lender for Partnership' at the Legal & General Mortgage Club Awards.

As a result of our focus on delivering great service, we have seen a 60% increase in our intermediary Net Promoter Score from +25 in 2014 to +40 in 2015.

Strategic Corporate Partners

In addition to relationships with Mortgage Intermediary Partners, we operate strategic partnerships that enable us to combine the Virgin Money philosophy, brand and core banking capabilities with partners' technical product expertise and infrastructure.

We launched our own in-house credit card business in conjunction with TSYS, a leading provider of payments platforms, in 2015. The combination of the Virgin Money brand and our in-house analytical capabilities, together with the scalability of the TSYS platform, provide both the volume capacity and the product capability to grow this business significantly.

We also partner with a number of providers to support our non-interest income product lines. This is particularly relevant when it is more efficient for us to partner with an established provider, than to build our own infrastructure. Examples of such partners are IFDS, who support our Investments and Pensions business and MAPFRE, for Travel Insurance. A full list of key Strategic Providers can be found in the table below.

STRATEGIC PARTNERS

Partner	Product	
TSYS	Credit Cards	Provides payments platform for the Virgin Credit Card.
IFDS and State Street Global Advisors	Investment and Pensions	Provide a full range of investment management and administration services in support of the Virgin Money Investments and Pensions business.
MAPFRE	Travel Insurance	Virgin Money Travel insurance is underwritten by MAPFRE, the multinational insurance and reinsurance company.
Ageas	Home and Motor Insurance	Provides sales, servicing, administration and claims management support for Virgin Money Home and Motor Insurance. Home insurance products are solely underwritten by Ageas Insurance Limited (AIL) and motor insurance is underwritten by a selected panel of insurers managed by AIL.
Friends Life	Life Insurance	Provides underwriting, sales, service and claims management support, complementing Virgin Money's distribution capabilities.
Monitise	Smartr	Connects banking, payments, and mobile to consumers via its Bank Anywhere, Pay Anyone and Buy Anything product suite.
Travelex	Travel Money	Exclusive travel money provider to Virgin Money.
World First	International Money Transfers	Provides white labelled foreign exchange services, offering Virgin Money customers a simple, speedy and safe way of transferring money overseas.

Delivering to our Stakeholders

Corporate Partners

We can't succeed without the trust and support of all our external stakeholders who include shareholders, regulators, the government and ratings agencies.

Aim

At Virgin Money we are committed to working responsibly and acting professionally with all of our external stakeholders.

Achievements in 2015

In 2015 our engagement with regulatory consultations and investigations included:

> working with the relevant authorities on the introduction of regulations connected to the Financial Services (Banking Reform) Act 2013;

> supporting the CMA investigation into the supply of PCA and SME banking services, reinforcing our viewpoint that the proposed remedies do not go nearly far enough to break the dominant position of the large incumbent banks in UK retail banking;

> supporting the FCA cash savings market study, and the remedies designed to improve disclosure, switching and convenience;

> supporting the FCA credit card market study and the proposed requirements for full transparency and responsible lending in the credit card market; and

> supporting the establishment of the PSR. We view access to payment systems as a key issue holding back competition in UK retail banking, especially in the PCA market.

Priorities for 2016

> maintain regular and transparent dialogue with shareholders and continue to broaden our shareholder base;

> maintain strong, open relationships with all of our regulators;

> continue to work with government agencies and other relevant organisations in the efforts to improve standards in the banking sector; and

> continue to engage with rating agencies to ensure they are well briefed on our strategic and financial performance.

Government and regulators

We engage regularly with UK government agencies and other bodies to assist in the formulation of public policy around consumer issues, competition in banking, financial inclusion and financial education.

Our vision for Virgin Money is to become a full-service retail bank that is able to compete effectively on a level playing field with the large incumbent banks.

However, we believe that a level playing field does not currently exist. As a result, we welcomed the central conclusion of the CMA's 'Summary of Provisional Findings Report', published in October 2015, that there is limited customer engagement and low switching in the personal current account market. We are concerned that the CMA's proposed remedies do not go nearly far enough to ensure that customers are better served in the future. We will continue to engage with the CMA ahead of publishing its final report.

Our continued focus on delivering on our promises and our conservative approach to financial and risk management has resulted in strong regulatory relationships. We will continue our approach of openness and transparency with our regulators in 2016.

Rating agencies

Rating agency feedback is an important consideration when formulating our ongoing strategy. We manage these relationships through regular interaction with Fitch and Moody's, the rating agencies.

In November 2015, the rating agency Fitch revised Virgin Money plc's outlook to Positive from Stable and affirmed its long-term rating at BBB+. Fitch noted our well-managed low risk profile, healthy asset quality and improving profitability.

Virgin Money Lounge, Glasgow

Delivering to our Stakeholders

Communities

Our Community activity raises awareness of the Virgin Money brand and business as a force for good and is an integral part of our commitment to building a bank where everyone is better off.

Aim

We are committed to supporting the communities in which we work, to help them flourish, both socially and economically.

Achievements in 2015

- £92.5 million, including Gift Aid, was donated to charities through Virgin Money Giving, our not-for-profit online donation service, 5% higher than in 2014;
- runners in the 2015 Virgin Money London Marathon raised £54.1 million for charity, up from £53.2 million in 2014, which set a new world record for an annual, single day charity fundraising event for the ninth successive year;
- the official charity of the 2015 Virgin Money London Marathon, Cancer Research UK, raised more than £3.7 million through its partnership with Virgin Money, £276,000 of which was raised by Virgin Money colleagues;
- the Virgin Money Foundation was launched in August 2015, with the first round of successful grant applications, totalling £900,000, announced in December 2015;
- over 245 schools and almost 11,000 young people participated in our Make £5 Grow programme and over 32,000 young people participated in the second Fiver Challenge; and
- colleagues volunteered 1,300 days to good causes.

Priorities for 2016

- continue to invest in Virgin Money Giving to increase online giving in the UK;
- grow the Virgin Money Foundation in the North East of England and, over time, across the UK;
- continue to invest in a range of programmes which support young people; and
- support colleagues engaging in local community projects.

£420 million

raised through Virgin Money Giving, including Gift Aid since launch in October 2009

Total Donations including Gift Aid

Note: By the end of 2015, £420 million, including Gift Aid, had been donated through Virgin Money Giving since its launch in October 2009. This figure includes Gift Aid claimed on donations, 100% of which was passed on to Virgin Money Giving's charity partners.

Our Community programme covers four key areas:

- fundraising;
- investing in education, employability and enterprise;
- supporting local communities; and
- supporting colleague engagement in their local communities.

Fundraising

Virgin Money Giving

In 2009, we launched Virgin Money Giving, our not-for-profit online donation service. Its ambition is simple – to help people raise more money for charity. Since its launch, £420 million has been raised for charities through Virgin Money Giving. More than 11,500 charities have registered with Virgin Money Giving and it is estimated that an extra £13.0 million has been raised for charities because of Virgin Money Giving's not-for-profit model.

The Virgin Money London Marathon

The Virgin Money London Marathon is the largest, one-day, annual fundraising event in the world. In 2015, the event raised a record-breaking £54.1 million for good causes, with over £22.1 million of that raised through Virgin Money Giving. This took the total amount raised by runners to more than £770 million since the event was founded in 1981.

"2015 was a big year for Cancer Research UK. We were the official charity of the Virgin Money London Marathon for the first time, and our runners raised money to help build the Francis Crick Institute, a pioneering medical research institute in central London.

"Cancer Research UK's marathon team set a fundraising target of £2.5 million to support the Francis Crick Institute and I am delighted to say that, with the support of Virgin Money, we hit £3.7 million in total.

"When it opens in 2016, the Francis Crick Institute will be game-changing for medical research and will help us to get a better understanding of a range of diseases, including cancer, which will help us treat them more effectively in the future."

Sir Harpal Kumar
Chief Executive
Cancer Research UK

Virgin Money London Marathon 2015 finishers medals

Delivering to our Stakeholders

Communities

Charity of the Year
Chosen by colleagues, our Charity of the Year for 2014/2015 and the official charity of the 2015 Virgin Money London Marathon was Cancer Research UK. Cancer Research raised over £3.7 million through its partnership with Virgin Money, including £276,000 raised by Virgin Money colleagues. The money raised helped to build the Francis Crick Institute – a world leading centre of biomedical research and innovation, due to open in 2016. Our Charity of the Year for 2015/2016 and the official charity of the 2016 Virgin Money London Marathon is the NSPCC.

Investing in education, employability and enterprise

Make £5 Grow
Make £5 Grow is Virgin Money's enterprise education programme which aims to give young people aged between nine and 11 years old the experience of starting a small business using a £5 loan from Virgin Money. Now in its fourth year, Make £5 Grow gives pupils an insight into how business works and helps them to build skills for the future. In 2015, over 245 schools and over 11,000 pupils participated, taking the total number of participants in the programme since its launch to more than 22,000.

Fiver Challenge
To complement the Make £5 Grow programme we continued our partnership with Young Enterprise to deliver the government-backed 'Fiver Challenge' – a national competition for primary schools aimed at introducing the world of enterprise to young people. Young people are provided with a pledge of £5 to set up small businesses or create products and services they can sell or deliver at a profit. Almost 500 schools and nearly 32,000 pupils participated in the programme in 2015.

Both Make £5 Grow and the Fiver Challenge give us the opportunity to engage with the next generation of customers and support our quest to build a better bank.

LifeSavers
The 'LifeSavers' programme supports primary schools to embed financial education within the whole school curriculum and encourages parents and the wider community to be actively involved in children's financial education. Savings clubs are set up in partnership with the local credit union with children encouraged to save small, regular amounts of money each week and to set themselves savings goals. The expansion of the 'LifeSavers' programme, and Virgin Money's support, was announced in January 2016. More than 40,000 children across the country will be able to take part in the programme over the next three years.

Supporting local communities

Virgin Money Foundation
In August 2015, Virgin Money launched the Virgin Money Foundation (the 'Foundation') – a new, independent charitable foundation that will focus initially on community projects in the North East of England, and over time will grow to operate nationally.

The Foundation promotes the sustainable regeneration of economically and socially deprived communities in the UK. This will include providing social investment in community housing and building projects, promoting opportunities for youth work and training, as well as investing in projects designed to relieve unemployment.

The Government has committed £4 million of funding – £1 million per year for four years – to be granted through the Foundation to support charitable projects in the North East of England. Virgin Money is matching the Government's donation. This means that the Foundation has £8 million of committed funding.

The Edinburgh International Festival Fringe and Fireworks
Virgin Money is proud to support the Edinburgh Festival Fringe, the largest arts festival in the world. We sponsor the Fringe street events which take place on the Royal Mile and The Mound, enabling many thousands of visitors from Edinburgh and across the globe to enjoy hundreds of free shows. Virgin Money is also the principal sponsor of the Fireworks Concert, which brings the Edinburgh International Festival to a spectacular close. The 2015 Fireworks Concert was watched by 250,000 spectators.

Supporting colleague engagement in their local communities

Virgin Money actively encourages colleagues to support their local communities, as well as local and national charities. In 2015, colleagues volunteered over 1,300 days to good causes. In addition, Virgin Money's nationwide network of Stores and Lounges held more than 200 charity and community events in 2015.

Business in the Community
Virgin Money is a member and an engaged supporter of Business in the Community. Virgin Money's Chief Executive, Jayne-Anne Gadhia, is currently a Board Director of Business in the Community and Chair of its Scottish Advisory Board.

Environment

We recognise that sound business management is inextricably linked to sound environmental management. At Virgin Money we are committed to taking positive actions that will eliminate the impact our activities have on the broader environment.

Aim

Our aim is to have Net Zero Greenhouse Gas (GHG) Emissions by 2030, protecting the environment by conducting our business in a sustainable, ethical and responsible way. We will contribute towards a low carbon, more resource efficient economy by measuring, monitoring and controlling consumption as part of our ambition to make 'everyone better off'.

Managing our emissions

We reported comprehensive data on GHG Emissions within Scope 1 and 2, and business travel within Scope 3, for the first time in 2014. We are pleased to be able to report a reduction of 10.7% over the year as a result of proactive management and investments made.

Virgin Money is required to report on GHG Emissions under the Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013 (the Regulations). The Group follows the principles of the Greenhouse Gas (GHG) Protocol Corporate Standard as of 31 December 2014 and Department for Environment, Food and Rural Affairs (DEFRA) Voluntary Reporting 2012 Guidelines (the Guidelines) to calculate its emissions in Scope 1, 2 and 3.

Reporting period

The reporting period for emissions corresponds with Virgin Money's financial reporting year, 1 January to 31 December.

Scope of disclosure

Virgin Money reports emissions based on its property portfolio. Reported Scope 1 emissions cover: emissions generated from the gas and oil used in all buildings from which the Group operates; emissions generated from Group-owned vehicles used for business travel; and fugitive emissions arising from the use of air-conditioning and chiller/refrigerant plant to service the Group's property portfolio. Reported Scope 2 emissions cover emissions generated from the use of electricity in all buildings from which the Group operates. Reported Scope 3 emissions relate to business travel undertaken by all colleagues using rail, private vehicles, hired vehicles, contracted taxi services and air travel.

Omissions

There are no omissions for either Scope 1 or 2 reporting.

Our voluntary reporting for Scope 3 includes travel booked through our corporate travel provider, personal expenses and contracted taxi usage. Currently we do not report on any other Scope 3 emissions.

Compliance with the Regulations

The Group has achieved full compliance with the Regulations for the whole of its property portfolio. The only estimated emissions relate to energy consumed in properties where the landlord controls the supply and recharges Virgin Money. In these instances (restricted to two properties) energy costs are split on a floor area basis.

Fugitive emissions for Virgin Money arise from the use of air conditioning and chiller/refrigerant equipment to service the Group's property portfolio. Leakage rate and emission factors from the Guidelines have been applied to each asset on the register according to the gas type used with the asset. This information is gathered and reported by the Group's maintenance supplier immediately on any gas leakage. This data is included within the Scope 1 segment of the GHG table listed below.

GHG emissions CO_2e tonnes

Scope	2015	2014
Scope 1*	1,868.7	1,781.0
Scope 2*	4,913.9	5,815.2
Scope 3	1,188.7	1,329.4
Total	**7,971.3**	**8,925.6**

Intensity ratio

Virgin Money has chosen to use an intensity ratio of GHG per Full Time Equivalent (FTE). FTE is straightforward to calculate and verify and also normalises consumption in a growing business. We are encouraged by the reduction of almost 22% in this ratio between 2014 and 2015.

Scope	2015	2014
GHG emissions per average FTE	2.61 tCO_2e	3.33 tCO_2e

Delivering to our Stakeholders

Environment

Independent assurance

Although not required by the Regulations, Virgin Money engaged KPMG LLP to undertake a limited assurance exercise using the assurance standards ISAE 3000 and ISAE 3410 over the GHG data highlighted in this report with a (*). KPMG has issued an unqualified opinion over the selected emissions data and their full assurance opinion is available on virginmoney.com[1].

Achievements in 2015

- refreshed our environmental policy and agreed the target to have net zero GHG emissions by 2030;
- fully complied with the requirements of the Energy Saving Opportunities Scheme (ESOS);
- commenced a programme of replacing all lighting with LED fittings across our property portfolio;
- secured 100% renewable energy for electricity contracts within our direct control;
- worked with key suppliers to promote sustainability, reduce environmental impact and enhance reporting capability;
- engaged with external bodies including the Major Energy Users Council, Energy Savings Trust and Business in the Community to help develop our strategic proposals; and
- started a programme of work with Carbon Credentials to baseline all of our current GHG Emissions under Scope 3.

Priorities for 2016

- finalise a transparent methodology to define total GHG Emissions for the Virgin Money Group;
- set out a clear plan, including interim targets, to achieve Net Zero GHG Emissions by 2030;
- raise awareness and profile of environmental initiatives across the Company to ensure that all colleagues are empowered to make a difference; and
- ensure all new and key suppliers understand fully the aims of the Company and the part they can play in reducing the impact their operations have on the environment.

Use of resources

Our systems and process to measure resources used are improving year on year and the table below shows actual consumption compared with 2014.

		2015	2014
Energy	Stated in Gwh	18.5	18.5
Stationery	% from environmentally sustainable sources	57.2	45.2
Travel	Total miles travelled	6.4m	6.5m
Waste	Tonnes produced % sent to landfill	532.9 6%	400.5 4%
Water	Cubic metres per FTE	18.7	16.5

Stationery – relates to purchases through approved supplier.

Travel – includes all air, rail, taxi and public transport processed through travel providers or claimed through expenses.

Waste – now includes Store and Lounge trade waste in addtion to main offices.

Water – consumption is for metered sites only and includes a significant leak at the main office site in Gosforth.

Our supply chain

In 2015, we continued to work with some of our key suppliers, in the areas we can influence, to ensure products and services used in our business are environmentally sound and that any waste is minimised. We look to build lasting relationships with companies who share our passion for protecting the environment. To support this we have added a number of small to medium sized enterprises to our supply chain to maximise our support for growing companies with sound environmental values.

1 The level of assurance provided for a limited assurance engagement is substantially lower than a reasonable assurance agreement. A summary of the work KPMG performed is included within their assurance opinion. Non-financial performance information, GHG quantification in particular, is subject to more inherent limitations than financial information. It is important to read the data in the context of KPMG's full statement and Virgin Money's reporting guidelines available at virginmoney.com.

Risk Overview

Effective risk management is a core part of our strategy. Virgin Money is a strong, customer-focused, low risk retail bank, unburdened by legacy issues. Our focus on maintaining a high-quality balance sheet is supported by our prudent risk appetite, our strong risk culture and our robust approach to risk management.

The amount and type of risk that we target and tolerate (our 'risk appetite') is reflected in our strategy and is designed to achieve an appropriate balance between risk and reward.

Risk as an enabler of growth, quality and returns

Our business strategy and risk appetite is focused on creating a business that can continue to grow strongly, maintain a high-quality balance sheet and deliver sustainable shareholder returns.

Risks are identified, managed and mitigated using our Risk Management Framework (see page 148). The principal risks which could impact the delivery of our strategy, are outlined on pages 50 to 53.

Commitment to balance sheet strength

We place great importance on maintaining a well capitalised business with a strong liquidity position. Our approach supports stable balance sheet growth, our credit rating, and Basel III requirements. The business plan is designed to mitigate the impacts of a range of stress tests including the UK variant stress, severe idiosyncratic stresses, liquidity stress tests and key sensitivities, while exceeding regulatory requirements.

Delivering asset quality

We maintain high-quality mortgage, credit card and wholesale portfolios. We continue to deliver strong asset quality as we grow our retail portfolios. Our lending meets performance targets which include asset quality guardrails.

95% of our wholesale portfolio is rated AA+ or above.

Funding and liquidity management

Our loan origination grows in line with available funding and we fund before we lend. Our funding plan is retail deposit led with diversification into wholesale funding. Our minimum level of High Quality Liquid Assets is calibrated to our view of liquidity risks reflected in the Board approved minimum liquidity requirement.

Market risk management

We do not operate a trading book and we have a limited appetite for market risk. Our Group Treasury Function ensures full measurement, management and control of interest rate risks, hedging all key exposures.

Risk decision making

Our approach to managing risk is designed to support the business in delivering sustainable growth. We have an integrated approach to business planning and combine achievable market share targets with prudent macroeconomic forecasts to ensure realistic growth targets. Board risk appetite is embedded in the activities of Risk teams, Commercial functions, Finance and Treasury. Our business plans are designed to generate a balanced mix of fee and interest income.

Risk culture

Our risk culture is aligned to our EBO philosophy and encourages accountability from each business area. A strong and independent Risk Function helps to ensure adherence to our risk management framework.

We are committed to nurturing a consistent risk culture throughout the business to support transparency and trust. Our risk culture is founded on a clear articulation of risk appetite, an effective governance structure and risk management framework, committed leadership, rapid escalation of threats or concerns and the sharing of information across the organisation.

Monitoring against risk appetite

Our risk analysis, management and reporting allow for opportunities as well as risks to be identified and ensure that they are managed in line with our appetite. Our principal risks and performance are monitored and reported regularly and are subject to appropriate stress testing. This allows for the risk at both an individual risk class and aggregate portfolio level to be assessed.

Robust risk management framework

Our approach to risk is fundamentally about a strong risk culture and clearly defined risk appetite and is reflected in the risk management framework. Our risk framework allows us to benefit from full engagement throughout the business in developing controls to ensure that the business operates within approved risk appetite and limits.

Risk Overview

Achievements in 2015

Credit ratings

In November 2015, rating agency Fitch revised Virgin Money plc's outlook to Positive from Stable and affirmed our long term rating as BBB+.

Wholesale funding

Our funding position remains strong with a loan-to-deposit ratio of 107.5%. During 2015 we saw an increase in our retail lending, the successful release of our £750 million Retail Mortgage Backed Securities (RMBS) programme, Gosforth Funding 2015-1, and the first issuance of £300 million Medium Term Notes.

Retail funding

During 2015, our deposits franchise continued to flourish. Deposit balances grew by 12% to £25.1 billion in 2015, a market share of 1.5%. Our deposit balances provide a strong and stable funding mix.

Credit card migration

During 2015 we completed the migration of over 675,000 customer records onto our newly built credit card infrastructure, completing our program to transfer our cards business from MBNA.

Regulatory change

Resolution and Recovery Plans were updated to reflect the requirements of the EU Bank Recovery and Resolution Directive, ahead of new rules coming into effect in January 2016. We have implemented the new Basel III Liquidity Coverage Ratio and applied for full regulatory permissions under the FCA Consumer Credit Sourcebook (CONC). We have made changes to our Advanced Internal Ratings Based capital models and refined our Pillar 2 approaches in the light of regulatory guidance.

Investment in infrastructure

Enhancements have been made to the Group's financial crime and information security systems to reflect the external threat landscape and evolving business strategy. In addition, a Chief Security Officer was appointed bringing us extensive experience in the field.

Priorities for 2016

Macro environment

As a UK retail bank we are focused on serving domestic customers and continue to support and benefit from the resilient UK economy and housing market. We are however, very aware of the downside risks related to the impending UK referendum on EU membership, the uncertain outlook for interest rates, and the recent market turbulence caused by the slowdown in emerging markets and falling commodity prices. All of these have the potential to adversely impact the UK economy. A lower for longer forecast interest rate puts pressure on net interest margins and therefore business and financial performance.

Wholesale funding

Our funding strategy is to access wholesale funding to supplement our core retail deposit base in order to optimise funding costs, extend tenor and ensure we have appropriate diversification in the funding base. As we develop our wholesale funding programmes, our mix of wholesale may rise, however, will remain relatively low as a proportion of overall funding. We have amended our risk appetite to accommodate a loan-to-deposit ratio of up to 115%, over time from 110%, as a result of our successful participation in the wholesale markets. In January 2016, Gosforth 2016-1 raised a further £803 million of funding across three tranches denominated in Sterling, Euros and U.S. Dollars. We plan to further improve wholesale diversification by issuing covered bonds in 2016.

Stable balance sheet growth

Our focus on asset quality and balance sheet efficiency continues as the business grows. Credit policy and decisioning systems are regularly reviewed and tested to ensure they develop in response to changes in customer and competitor behaviours, maintaining the quality of the portfolios. This work will continue throughout 2016.

Development of new product lines and delivery channels

Risk will continue to support the business in its strategic initiatives, including the development of our SME strategy and the enhancement of our digital capability, to ensure they are delivered within our risk appetite.

Buy-to-let

In December 2015, the BoE Financial Stability Report cited concerns over the growth in buy-to-let (BTL) lending and the impact that a structural shift to the private rental sector may have on market stability. In addition, there have been several tax and regulatory changes that may collectively weaken the attractiveness of BTL to an investor. These changes have added uncertainty to the outlook of BTL for both landlords and lenders, particularly over the medium to long-term. Our mortgage business remains high-quality and is comprised of 83% residential and 17% BTL mortgages. We focus on BTL for retail customers, rather than portfolio landlords, and our affordability and rental cover requirements are prudent.

Continued investment in infrastructure

We recognise the pace of change in the external threat environment and as such will continue to focus on development of capability to protect against cybercrime and invest in risk systems and frameworks to enable the further development of our digital offering.

Third party administration

We have a mature control environment regarding the oversight of key outsourcers and will continue to refine our operating model. As the number of business partnerships grows, our reliance on excellent execution from third parties necessitates more sophisticated approaches.

Regulatory change

Delivery of regulatory change programmes will be a core focus in 2016:

Regulation

- Ring-fencing: The Financial Services (Banking Reform) Act 2013 will result in the ring-fencing of retail and commercial banking operations to separate them from investment banking activities. Given that we are a UK focused retail bank, we expect our entire business will be within the ring-fence when it comes into effect at the beginning of 2019; and
- The Mortgage Credit Directive (MCD): The MCD aims to create an EU wide mortgage credit market with a high level of consumer protection. This includes new requirements for disclosure, foreign currency loans, training and competence, binding offers, APRs and cooling-off periods to be in force from March 2016.

Market Studies

- FCA Credit Card Market Study: Over the previous two years, the FCA has consulted firms as part of their Credit Card Market Study, investigating consumer driven competition, cost recovery and unaffordable credit card debt. The final outcomes of the study are expected to be reported in Spring 2016;
- FCA Cash Savings Market Study: Findings published in December 2015 propose remedies to improve disclosure, switching and convenience for customers in the retail savings market; and
- Competition Markets Authority (CMA) investigation into current account and business banking sectors: Provisional findings published in October 2015 proposed remedies focused heavily on switching, transparency and comparability. We will continue to engage with the CMA ahead of publishing its final report in May 2016.

Capital Consultations

- We are fully engaged in the Bank of England's consultation on minimum requirements for own funds and eligible liabilities (MREL) and regulatory buffers. Our capital planning assesses a range of outcomes from these consultations and the impact on our business plans. This allows for well informed capital planning.

IFRS 9

- We will develop new models and practices to meet the requirements of this new accounting standard in time for its application in 2018.

Risk Overview

Risk Governance

Board
Chairman: Glen Moreno

Board Committees[1]

Risk Committee	Audit Committee	Remuneration Committee
Chair: Colin Keogh (Non-Executive Director)	**Chair: Norman McLuskie** (Non-Executive Director)	**Chairman: Marilyn Spearing** (Non-Executive Director)

Executive Committees

Risk Management Committee	Asset and Liability Committee
Chairman: Chief Risk Officer Identifies and recommends risk appetite, manages risk within agreed limits, monitors key risk exposures in relation to risk strategy and recommends the approach to managing all types of risk.	**Chairman: Chief Financial Officer** Responsible for management and monitoring of liquidity, funding, capital and asset and liability management within agreed risk appetite and policy.

Management Committees

Operational Risk, Conduct Risk and Compliance Committee	Credit Risk Committee	Treasury Risk Committee

Functional Risk Boards

1 Additional Board Committees comprise Nomination Committee.

We manage risk strategy and appetite in tandem with overall strategy and use a comprehensive risk management framework tailored for each risk class. Mapping the risks that could affect the business both today and in the future allows a comprehensive and consistent approach across all business areas.

Effective governance is maintained through delegation of authority from the Board to the Executive, with committees designed to ensure our risk management approach is fully aligned with regulatory requirements and good industry practice.

The Board approved risk appetite incorporates the Board's tolerance for risk in pursuit of achieving our strategic objectives. Executive committees manage the business within the defined risk appetite and associated limits.

We use a 'Three Lines of Defence' model which defines clear responsibilities and accountabilities and ensures appropriate segregation of duties and effective independent assurance.

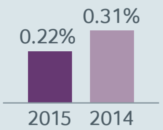

Virgin Money Lounge, Manchester

Risk Overview

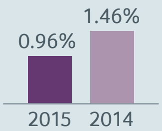
Risk Governance

Principal risks	Key mitigating actions
Credit Risk We provide residential and BTL mortgages and credit cards to customers across the UK. There is a risk that any adverse changes in the economic and market environment and/or the credit quality or behaviour of borrowers results in additional impairment losses thereby reducing profitability. Wholesale exposures arise through the use of derivative instruments to manage interest rate risk and the liquid asset portfolio.	› credit risk is managed through risk appetite and risk limits reflected in approved credit policy; › a robust credit risk framework helps ensure that the credit quality and composition of the portfolios remain within risk appetite limits. This is monitored and reported through governance committees regularly; › stress and scenario testing allows us to confirm portfolio resilience; › credit risk metrics are benchmarked against competitors and industry averages; and › credit risk arising from derivative and from securities financing transactions is mitigated by collateralising exposures on a daily basis.
Market Risk Market risk is the risk that unfavourable market moves lead to a reduction in earnings or value. We do not trade or make markets. Interest rate risk is the only material category of market risk for the Group.	› market risk is managed through Board approved risk appetite limits and policy; › we mitigate exposures through the use of natural offsets and derivatives; and › stress and scenario testing focuses on the impacts of differing interest rate environments.
Operational Risk Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk. The management of third party relationships, cybercrime and information security remain a key focus for us.	› risk appetite is focused on maturing the control environment and therefore managing operational risk; › a programme of investment in security infrastructure is in place to mitigate threats including cyber attack; › we continue to invest in and develop risk management frameworks, systems and processes; and › we monitor external events impacting other financial services companies to inform stress testing.
Conduct Risk and Compliance Conduct and compliance risk is defined as the risk that the Group's operating model, culture or actions result in unfair outcomes for customers, and the risk of regulatory sanction, material financial loss or reputational damage if the Group fails to design and implement operational processes, systems and controls and maintain compliance with all applicable regulatory requirements.	› compliance is maintained through an effective and timely response to changes in the regulatory environment; › the customer is placed at the heart of decision-making by ensuring fair outcomes through comprehensive risk assessment and testing; › we continue to invest in and develop risk management frameworks, systems and processes; and › we focus on training to ensure colleague performance aligns with customer accountabilities and provides awareness of vulnerable customers' needs.

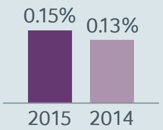
Key risk indicators



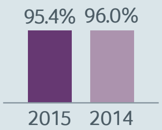
3+ Arrears – Mortgages



2+ Arrears – Cards



Provisions as a % of customer balances



Wholesale % AA+ or above

Commentary

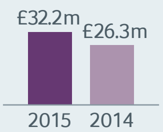
2015 has seen improved arrears performance and favourable HPI movements.

Wholesale credit performance remains stable with 95% of counterparties rated AA+ or above.

Future focus

Continued delivery of strong asset quality aligned to growth of the mortgage and cards books.

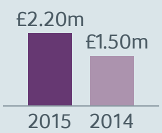
Maintain our 'no loss' position for the wholesale credit portfolio.



IRRBB – Capital at Risk

Capital at Risk has increased in a positive rate shock scenario following growth in fixed rate assets and liabilities, reflecting the risk that they terminate their contract prior to the end of the fixed rate period. This remains within risk appetite.

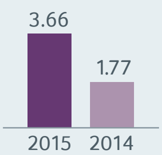
Refine our interest rate risk management systems and approaches.



Operational Losses

As expected, following the set-up of the cards business, the absolute amount of losses increased, but is low and remains within risk appetite.

Continued investment in cybercrime defence, along with fraud and anti-money laundering infrastructure.



Total Complaints (per 1,000 accounts)

The increase in total complaints is due to the migration of the credit card portfolio which has a complaints rate of 6.09 per 1,000 accounts.

Continue to protect the Group's position with limited exposure to conduct risk.

Risk Overview

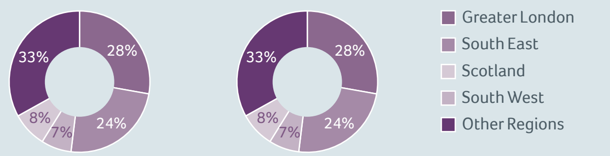
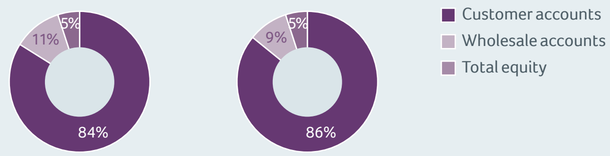
Risk Governance

Principal risks	Key mitigating actions	
Strategic and Financial Risk Strategic risk is the risk of significant loss or damage arising from business decisions that impact the long-term interests of stakeholders or from an inability to adapt to external developments. Financial risk is focused primarily on concentration risk. Credit concentration risk is managed for retail and wholesale credit exposures at portfolio, product and counterparty levels.	› Board focus is on ensuring alignment of business development and planning with risk appetite; › we invest in processes, systems, recruitment and training to support new business developments;	› we use robust risk and project management disciplines to ensure that implementation is delivered safely; › active focus is on asset origination and portfolio management to eliminate inappropriate concentration risk; and › regular validation and review of models is performed.
Funding and Liquidity Risk Liquidity risk represents the inability to accommodate liability maturities and withdrawals, fund asset growth, and otherwise meet contractual obligations to make payments as they fall due. Funding risk represents the inability to raise and maintain sufficient funding in quality and quantity to support the delivery of the business plan.	› Board approved risk appetite and funding and liquidity policy define a limit structure; › liquid resources are maintained in adequate quantity and quality to meet estimated outflows;	› a prudent mix of funding sources is maintained with a maturity profile set in risk appetite and policy limits; and › stress and scenario testing considers threats to funding plans and changes in consumer behaviour.
Capital Risk Capital risk is defined as the risk that the Group has a sub-optimal amount or quality of capital or that capital is inefficiently deployed across the Group.	› Board approved risk appetite ensures we are holding sufficient capital within regulatory requirements; › the capital management policy sets out minimum standards;	› capital procedures are subject to independent oversight; and › stress and scenario testing assesses capital adequacy under a range of severe market wide stress scenarios and idiosyncratic stress events.

Viability Statement

In accordance with the UK Corporate Governance Code, the directors have assessed the viability of the Group over a three year period, taking into account the Group's current position and the potential impact of the principal risks and uncertainties, influencing the priorities for 2016, which are set out on pages 45 to 53. Based on this assessment, the directors confirm that they have reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due in the period to 31 December 2018.

The directors have determined that a three year period to 31 December 2018 constitutes an appropriate period over which to provide its viability statement. This is the period focused on by the Board during the strategic planning process. Whilst the directors have no reason to believe the Group will not be viable over a longer period, given the inherent uncertainty involved, we believe this presents users of the Annual Report with a reasonable degree of confidence while providing a longer term perspective.

Key risk indicators	Commentary	Future focus
 Mortgage concentration 2015; Mortgage concentration 2014	We apply lending policy restrictions which predominantly affect regions where we have concentrations of credit risk.	Focus on development of our customer proposition and digital capability.
 Funding mix 2015; Funding mix 2014	Improved balance sheet efficiency and diversity of funding were achieved through RMBS and MTN issuance.	Continue to improve balance sheet efficiency and resilience through measured diversification of wholesale funding.
Capital metrics (see table below)	We have made improvements in risk-weighted asset calculation methodologies which contributed to improved capital efficiency.	Continue to maintain a high-quality capital base with ratios in excess of regulatory requirements.

Capital metrics

	2015 %	2014 %
CET1	**17.5**	19.0
Leverage ratio	**4.0**	4.1

In making this statement, the Board carried out a robust assessment of the principal risks facing the Group, including those that would threaten its business model, future performance, solvency or liquidity. As described in the Corporate Governance Report on pages 81 to 110 and Risk Management Report on pages 140 to 142, the Board monitored the Group's risk management and internal control systems, and carried out a review of their effectiveness. The monitoring and review covered all material controls, including financial, operational and compliance controls.

The Board considers annually, and on a rolling basis, a three year strategic plan. The output of this plan is used to perform stress analysis including a review of the sensitivity to business as usual risks, such as profit growth and other severe but plausible events. The Board also considers the ability of the Group to raise finance and deploy capital. These results take account of the availability and likely effectiveness of the mitigating actions that could be taken to avoid or reduce the impact or occurrence of the underlying risk.

As part of the Internal Capital Adequacy Assessment process (ICAAP) and Internal Liquidity Adequacy Assessment (ILAA), we perform a wide range of severe macro-economic and idiosyncratic stress tests. The results of our stress testing show that sufficient capital is held to cover the stress scenarios and liquid resources, both in amount and quality, to survive them. Supporting capital and funding plans were developed to survive the impact of the stress scenarios over the planning horizon to 31 December 2018.

Financial results

Paula Radcliffe at the Virgin Money London Marathon 2015

Summary of Group results

Underlying basis – consolidated income statement

	2015 £m	2014 £m	Change %
Net interest income	**456.1**	366.1	25%
Other income	**67.0**	72.1	(7)%
Total income	**523.1**	438.2	19%
Costs	**(332.5)**	(317.6)	5%
Impairment[1]	**(30.3)**	(15.8)	92%
Underlying profit before tax	**160.3**	104.8	53%

1 Net of debt recoveries.

Consolidated balance sheet

	2015 £m	2014 £m	Change %
Assets			
Cash and balances at central banks	**888.6**	851.3	4%
Loans and receivables	**27,724.6**	23,822.2	16%
Available-for-sale financial assets	**1,296.9**	1,539.6	(16)%
Other	**318.9**	323.7	(1)%
Total assets	**30,229.0**	26,536.8	14%
Liabilities and equity			
Deposits from banks	**1,298.7**	846.7	53%
Customer deposits	**25,144.9**	22,365.7	12%
Debt securities in issue	**2,039.4**	1,594.1	28%
Other	**397.3**	477.2	(17)%
Provisions	**8.4**	9.3	(10)%
Total liabilities	**28,888.7**	25,293.0	14%
Total equity	**1,340.3**	1,243.8	8%
Total liabilities and equity	**30,229.0**	26,536.8	14%

Basis of preparation of financial results

In order to present a more meaningful view of business performance, the results of the Group and its divisions are presented on an underlying basis of reporting as described below.

The following items have been excluded from underlying profits:

- additional Northern Rock consideration;
- other costs associated with IPO including share based payment charges; and
- strategic items and compensation for senior leavers.

Our Treasury function is not managed as a profit centre. Interest expense incurred from its funding and liquidity operations is allocated to the business divisions.

Financial results

Summary of Group results

Key ratios

		2015	2014	Change
Net interest margin	%	**1.65**	1.50	15bps
Cost:income ratio[1]	%	**63.6**	72.5	(8.9)pp
Cost of risk[2]	%	**0.12**	0.07	5bps
Statutory basic earnings per share	p	**22.9**	(0.4)	23.3 pence
Tangible net asset value per share	£	**2.54**	2.36	18 pence
Loan-to-deposit ratio	%	**107.5**	102.8	4.7pp
Common Equity Tier 1 ratio	%	**17.5**	19.0	(1.5)pp
Leverage ratio	%	**4.0**	4.1	(0.1)pp
Return on tangible equity	%	**10.9**	7.4	3.5pp

1 Including FSCS levy.

2 Defined as impairment charges net of debt recoveries divided by average gross balances for the period.

Key ratios are presented on an underlying basis except where stated.

Reconciliation to statutory profit

	2015 £m	2014 £m	Change %
Underlying profit before tax	**160.3**	104.8	53%
Additional Northern Rock consideration	**–**	(36.0)	(100)%
Other costs associated with IPO including share based payment charges	**(10.5)**	(28.4)	(63)%
Strategic items	**(8.1)**	(6.4)	27%
Compensation for senior leavers	**(3.7)**	–	–
Statutory profit before tax	**138.0**	34.0	306%

Overview

Virgin Money is a simple business where the performance is driven by:

- Growth – our ability to add both assets and liabilities at high quality while maintaining margin development;
- Operational leverage – our platform of systems, people and processes can scale business volumes without parallel scaling of costs; and
- Quality – controlled via rigorous underwriting, supporting capital management and a low cost of risk.

Despite the external headwinds from the flat base rate environment and market pressures on mortgage margins, the business was able to deliver against all these driving factors – with strong balance sheet growth and net interest margin improvements, continued cost management and controlled development of the cost of risk. This allowed us to deliver an increase in underlying profit before tax of 53% compared to 2014, rising by £55.5 million to £160.3 million. As a consequence, return on tangible equity improved to 10.9% from 7.4%.

Summary of Group results

Strong balance sheet growth

	At 31 Dec 2015 £m	At 31 Dec 2014 £m	Change
Loans and advances to customers	**27,109.0**	23,093.1	17%
Funded assets[1]	**27,885.1**	24,181.9	15%
Customer deposits	**25,144.9**	22,365.7	12%
Wholesale funding	**3,314.3**	2,429.4	36%
Wholesale funding <1 year maturity	**1,274.9**	835.3	53%
Loan to deposit ratio	**107.5%**	102.8%	4.7pp
High Quality Liquid Assets[2]	**4,238.6**	4,235.9	–

1 Loans and advances to customers and banks, encumbered available-for-sale assets and encumbered cash and balances with central banks.

2 Level 1 + 2a + 2b. See Risk Management Report page 197 for definition. These include Funding for Lending drawings which are held off balance sheet but are available for repo and hence count towards liquidity resources.

During the year, we grew customer deposit balances by 12% or £2.8 billion, well in excess of market growth of 7%. Similarly, mortgage balances grew by 16% to £25.5 billion, significantly ahead of market growth of 1.8%, and our cards book increased by 44% to £1.6 billion.

We have a strong and increasingly diversified funding base. Residential Mortgage Backed Security (RMBS) notes in issue increased by £147.8 million to £1,741.9 million during 2015. This was as a result of the successful completion of the Gosforth Funding 2015-1 transaction in June 2015 which more than offset the paying down of outstanding funding from prior transactions.

In April 2015, we issued £300 million of senior unsecured debt, our debut issuance under our Global Medium Term Note (MTN) programme. The issue of MTN and RMBS further diversified our funding sources in line with the aim of wholesale funding providing up to 20% of total funding. They also provided term funding at a cost lower than retail funding of equivalent size and tenor.

In addition to non-retail funding on the balance sheet, we accessed the Government's Funding for Lending Scheme (FLS), with £0.7 billion drawn during the year to support lending growth and liquidity. Our total drawings from the Funding for Lending Scheme at 31 December 2015 were £3.0 billion, of which £0.8 billion was collateralised funding included within wholesale funding in the table above. If all FLS funding were on balance sheet, total non-retail funds would have represented 20% of total funding at the end of 2015. All Funding for Lending Scheme drawings remain off balance sheet unless used as collateral to support wholesale funding.

As our balance sheet consists predominantly of long-term mortgage assets, we do not rely on short-term wholesale funding which can introduce refinancing risk. Funding provided by retail deposit customers represented 83.2% of total liabilities and equity at the end of 2015.

Given our successful participation in the wholesale markets, we have amended our risk appetite to accommodate a loan-to-deposit ratio of up to 115% over time. This will support our aim of increasing balance sheet efficiency and funding diversification. During 2015, the loan-to-deposit ratio increased to 107.5% from 102.8% at the end of 2014.

We maintain a portfolio of High Quality Liquid Assets which consists mainly of deposits held at the Bank of England and UK Government bonds and is available to meet cash and collateral outflows.

Our liquidity position remains strong, with High Quality Liquid Assets of £4,238.6 million at 31 December 2015 compared to £4,235.9 million at 31 December 2014. High Quality Liquid Assets represent approximately 3.3 times our wholesale funding with a maturity of less than one year, providing a substantial buffer in the event of an extended market dislocation. In addition, we undertake regular stress tests of our liquidity position against a range of stress scenarios which further ensure that a robust level of High Quality Liquid Assets is maintained at all times.

The Liquidity Coverage Ratio (LCR) became the Pillar 1 standard for liquidity in the UK from October 2015. Our LCR at 31 December 2015 was 202%. This compares to the requirement of 80% set by the PRA which took effect from 1 October 2015. The requirement will increase to 100% from 1 January 2018.

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Financial results

Summary of Group results

Income benefited from growth and margin development

	2015 £m	2014 £m	Change
Net interest income	**456.1**	366.1	25%
Other income	**67.0**	72.1	(7)%
Total income	**523.1**	438.2	19%
Net interest margin	**1.65%**	1.50%	15bps
Average interest earning assets	**27,577**	24,475	13%

Net interest income increased by 25% in 2015, to £456.1 million. Just over half of this growth was driven by strong balance growth across mortgages and cards, the rest being a consequence of margin improvements. The improvement in net interest margin (NIM) to 1.65% in 2015 was mainly driven by management of the retail cost of funds, against a background of falling deposit interest rates across the market. Increasing the use of cost effective wholesale funding also contributed to NIM improvement. This was partially offset by pressure on mortgage pricing across that market, mitigated by our focus on higher yielding segments within our risk appetite. Lastly, although the margin on our credit card book reduced (as expected given the growth in the number of front book customers), at a group level having proportionately more credit cards drives a higher NIM.

Other income was 7% or £5.1 million lower at £67.0 million, primarily driven by the anticipated absence of card origination commissions as we changed our business model. Overall, our cards business contribution increased.

Costs remain tightly controlled

	2015 £m	2014 £m	Change
Costs[1]	**332.5**	317.6	5%
Cost:income ratio[1]	**63.6%**	72.5%	(8.9)pp
Cost:income ratio[2]	**61.2%**	68.7%	(7.5)pp

1 Including FSCS levy.

2 Excluding FSCS levy.

With costs (including the FSCS levy) of £332.5 million in 2015, cost growth during the year was limited to 5% despite a 15% increase in total customer balances, whilst maintaining levels of investment spend. This combined with our income increase of 19% produces positive JAWS at 14% and drove the cost:income ratio down by 8.9 percentage points to 63.6%. The table above also shows the cost:income ratio on the same basis as presented in 2014, which excluded the FSCS levy.

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Summary of Group results

Impairment reflects rigorous underwriting controls

	2015 £m	2014 £m	Change
Mortgages			
Impairment charge	**3.0**	1.2	150%
Cost of risk	**0.01%**	0.01%	–
Cards			
Impairment charge (gross of debt recoveries)	**34.2**	23.5	46%
Impairment charge (net of debt recoveries)	**27.3**	14.6	87%
Cost of risk (gross of debt recoveries)	**2.50%**	2.43%	7bps
Cost of risk (net of debt recoveries)	**2.00%**	1.51%	49bps
Group			
Impairment charge (gross of debt recoveries)	**37.2**	24.7	51%
Impairment charge (net of debt recoveries)	**30.3**	15.8	92%
Cost of risk (gross of debt recoveries)	**0.15%**	0.11%	4bps
Cost of risk (net of debt recoveries)	**0.12%**	0.07%	5bps
Impaired loans as a % of loans and advances	**0.4%**	0.5%	(0.1)pp
Provisions as a % of impaired loans	**35.6%**	29.5%	6.1pp

The cost of risk for mortgages was flat on 2014 at 0.01% in 2015 with the impairment charge increase of £1.8 million driven by a larger mortgage book. This stability reflected the continued high asset quality of the loan portfolio and a further reduction in the low level of defaults.

The impairment charge for credit cards, before debt sales, increased broadly in line with the size of the book. Net of debt sale recoveries, the charge increased by 87% to £27.3 million. In addition to book growth, this was a consequence of 2014 including the sale of charged-off credit card balances from both 2013 and 2014. The resulting cost of risk for credit cards net of debt sale recoveries increased by 49bps to 2.00% in 2015, from 1.51% in 2014.

Impaired loans as a percentage of loans and advances reduced to 0.4% at 31 December 2015 from 0.5% at 31 December 2014. Provisions as a percentage of impaired loans increased to 35.6% at 31 December 2015, from 29.5% at 31 December 2014. This rise was primarily due to portfolio growth in both mortgage and credit card lending, combined with a reduction in impaired balances in the mortgage book.

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Financial results

Summary of Group results

Statutory profit

Our statutory profit before tax of £138.0 million for 2015 compared to a statutory profit before tax of £34.0 million in 2014. This increase was primarily as a result of increased income, continued cost management, controlled development of the cost of risk and a reduction in non-recurring items in 2015. The non-recurring items in 2014 were mainly one-off Initial Public Offering transaction costs.

	2015 £m	2014 £m
Underlying profit	**160.3**	104.8
Costs associated with IPO:		
– Additional Northern Rock consideration	**–**	(36.0)
– IPO costs	**–**	(12.6)
– IPO share based awards and one-off payments on listing	**(10.5)**	(11.3)
– Premium on repurchase of Non-core Tier 1 notes	**–**	(4.5)
	(10.5)	(64.4)
Strategic items:		
– Strategic investment costs	**(7.4)**	(9.0)
– Gain on sale of subsidiary	**–**	4.5
– Loss for the year of disposal group	**–**	(1.0)
– Fair value adjustments	**(0.7)**	(0.9)
	(8.1)	(6.4)
Compensation for senior leavers	**(3.7)**	–
Profit before tax – statutory	**138.0**	34.0
Taxation	**(26.8)**	(25.3)
Profit for the year – statutory	**111.2**	8.7
Basic earnings per share – statutory (pence)	**22.9**	(0.4)

Strategic items

We incurred strategic investment costs of £7.4 million in 2015, which primarily related to investment in our credit card and digital platforms. These are considered to be significant non-recurring investment costs, so have been excluded from underlying profit.

Compensation for senior leavers

Compensation for senior leavers includes costs associated with senior employees who left the business during the year. These costs include accelerated share based payment charges. These are non-recurring items that are not considered part of the underlying results.

Taxation

Our effective tax rate in 2015 was 19.4%. The overall tax rate for UK banks will rise by 8 percentage points to 28% in 2016 as a result of the bank tax surcharge announced in the 2015 Summer Budget.

The surcharge increased the value of our deferred tax assets (other than those due to brought forward losses which cannot be offset against the bank tax surcharge). Recognising that increase resulted in a one-off credit to our tax charge of £2.6 million which reduced our effective tax rate below the 20.25% statutory rate of corporation tax in 2015.

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Summary of Group results

Growing return on assets and tangible equity

		2015	2014	Change
Return on tangible equity	%	**10.9**	7.4	3.5pp
Return on assets[1]	%	**0.37**	0.03	34bps

1 Statutory basis.

Return on tangible equity increased to 10.9% in 2015 from 7.4% in 2014, primarily due to increased profitability resulting from improved net interest margin and growth in balances. Statutory return on assets grew by 34 basis points to 0.37% in 2015, from 0.03% in 2014 due to growth in statutory profitability outpacing total asset growth, reflecting our operational leverage.

Strong capital structure

		2015	2014	Change
Capital ratios and risk-weighted assets				
Common Equity Tier 1 capital (CET1)	£m	**1,070.0**	980.5	9%
Risk-weighted assets (RWAs)	£m	**6,110.4**	5,160.6	18%
Common Equity Tier 1 ratio	%	**17.5**	19.0	(1.5)pp
Tier 1 ratio	%	**20.1**	22.0	(1.9)pp
Total capital ratio	%	**20.2**	22.1	(1.9)pp
Leverage ratio	%	**4.0**	4.1	(0.1)pp

Our Common Equity Tier 1 ratio was 17.5% at year end, compared with 19.0% at the end of 2014. The reduction reflects our increased capital efficiency with CET1 capital increasing by 9% whilst RWAs increased by 18%. The RWA increase was driven by strong asset growth, partially offset by a reduction in RWAs due to a change in our AIRB models. As a result, mortgage RWAs grew by only 15% in 2015 to £4,284.5 million compared to mortgage balance growth of 16%.

Our total capital ratio was 20.2% at 31 December 2015, reduced from 22.1% in 2014 as a result of the same underlying effects as CET1.

Our leverage ratio was 4.0% at the end of 2015, compared with 4.1% at the end of 2014, due to the increase in leverage ratio eligible assets.

Dividend

An interim dividend for 2015 of 1.4 pence per ordinary share was paid to shareholders on 9 October 2015. The Board has recommended a final dividend of 3.1 pence per ordinary share in respect of 2015 which will be paid, subject to approval at our AGM, in May 2016. Our intention is to pay an interim and final dividend for 2016, subject to performance.

Conclusion

We have delivered further growth in customer balances, diversified our funding base, retained a high quality balance sheet and increased returns in 2015. This progress, while maintaining strong capital ratios, positions us well to continue growing our business within our prudent risk appetite and has enabled the Board to recommend a final dividend in respect of 2015.

Dave Dyer
Chief Financial Officer

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Financial results

Divisional results

Segmental analysis

	Mortgages & Savings £m	Credit Cards £m	Current Accounts, Insurance & Investments £m	Central Functions £m	Group £m
2015					
Net interest income	358.5	97.6	–	–	456.1
Other income	2.5	18.0	36.6	9.9	67.0
Total income	361.0	115.6	36.6	9.9	523.1
Total costs	(92.7)	(37.1)	(16.7)	(186.0)	(332.5)
Gross impairment charge	(3.0)	(34.2)	–	–	(37.2)
Debt sale recoveries	–	6.9	–	–	6.9
Net impairment charge	(3.0)	(27.3)	–	–	(30.3)
Underlying Contribution	265.3	51.2	19.9	(176.1)	160.3
Net interest margin	1.52%	8.22%	–	–	1.65%
Cost of risk (Gross)	0.01%	2.50%	–	–	0.15%
Cost of risk (Net)	0.01%	2.00%	–	–	0.12%
Key balance sheet items at 31 December 2015					
Loans and advances to customers[1]	25,453.5	1,578.7	0.1	–	27,032.3
Customer deposits	24,914.6	–	230.3	–	25,144.9
Total customer balances	50,368.1	1,578.7	230.4	–	52,177.2
Risk-weighted assets	4,284.5	1,334.7	51.6	439.6	6,110.4

1 Excluding fair value of portfolio hedging.

Divisional results

	Mortgages & Savings £m	Credit Cards £m	Current Accounts, Insurance & Investments £m	Central Functions £m	Group £m
2014					
Net interest income	291.0	75.1	–	–	366.1
Other income	3.1	25.2	32.8	11.0	72.1
Total income	294.1	100.3	32.8	11.0	438.2
Total costs	(85.7)	(40.5)	(13.5)	(177.9)	(317.6)
Gross impairment charge	(1.2)	(23.5)	–	–	(24.7)
Debt sale recoveries	–	8.9	–	–	8.9
Net impairment charge	(1.2)	(14.6)	–	–	(15.8)
Underlying contribution	207.2	45.2	19.3	(166.9)	104.8
Net interest margin	1.42%	9.60%	–	–	1.50%
Cost of risk (Gross)	0.01%	2.43%	–	–	0.11%
Cost of risk (Net)	0.01%	1.51%	–	–	0.07%
Key balance sheet items at 31 December 2014					
Loans and advances to customers[1]	21,887.5	1,098.2	0.1	–	22,985.8
Customer deposits	22,164.1	–	201.6	–	22,365.7
Total customer balances	44,051.6	1,098.2	201.7	–	45,351.5
Risk-weighted assets	3,729.8	973.2	47.2	410.4	5,160.6

1 Excluding fair value of portfolio hedging.

Financial results

Divisional results

Mortgages and Savings

We provide mortgages and savings to more than 1.5 million customers. Mortgages are sold primarily through our intermediary partners and savings primarily sold direct to customers through our digital channel.

Our Mortgage and Savings business remains the key profit driver for our business, contributing 69% of total income in 2015.

Mortgage Strategy

In what remains a very competitive market, our approach to mortgages is very straightforward. We offer a wide range of mortgage products supported by excellent service, primarily through our intermediary partners and supplemented by direct distribution.

Product development for mortgages is focused on growing our market presence in stronger yielding sectors where we are currently under represented, whilst respecting our existing prudent risk appetite. We aim to maintain our stock share for buy-to-let mortgages in line with the overall market.

We will continue to strengthen our intermediary proposition to build upon our existing intermediary relationships. Additionally, we will continue to invest in the retention of our existing customers.

Savings Strategy

Our savings products are simple and transparent, with no hidden catches. We have avoided 'teaser' products with bonus rates which subsequently fall to sub-market levels and provoke customer churn. Instead, we encourage customer retention with enduring, good value offers.

We offer customers a range of competitively-priced instant access and fixed term savings products, both available as ISAs, through all our channels: store, online, digital, postal and telephone.

Key developments – Mortgages

- we were pleased to deliver strong growth in mortgage balances in 2015, which increased by 16% to £25.5 billion at the year end, comfortably outperforming growth in the market of 1.8% over the same period;
- prime residential balances grew by 12% to £21.1 billion representing 83% of the overall mortgage book and 75% of new lending in 2015;
- buy-to-let balances of £4.4 billion represented 17% of the overall mortgage book at year end;
- the overall growth in balances was driven by strong new lending of £7.5 billion in the year to 31 December 2015. This represented an increase of 29% on 2014 and was equivalent to a 3.4% market share of gross lending, up from 2.8% for 2014;
- we successfully retained 67% of customers with maturing fixed rate or tracker products;
- we delivered year-on-year net lending growth of 53% in 2015, with net lending of £3.6 billion. This equated to a 10.6% market share of net lending, comparing favourably with 9.8% in 2014;
- our refreshed intermediary proposition was launched in February 2015 and the changes have been very well received by intermediaries, as evidenced by the 60% increase in NPS score from +25 in 2014 to +40 in 2015;
- we are committed to helping customers achieve their home ownership aspirations and made a number of enhancements to our First Time Buyer and New Build propositions during the year. The response from customers has been very positive, with the value of gross lending to these segments increasing by 59% year-on-year in 2015; and
- our mortgage impairment charge of £3 million reflects our conservative risk appetite, strong risk management and resulting high-quality mortgage book. Impaired loans as a percentage of loans and advances reduced to 0.4%.

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Divisional results

Key developments – Savings

- we grew retail savings balances by 12% to £24.9 billion at 31 December 2015, up from £22.2 billion at 31 December 2014;
- we opened more than 300,000 new savings accounts in the year and in May 2015 we opened our one millionth savings account since the acquisition of Northern Rock in January 2012;
- at year end we had more than 1.2 million savings customers and balances were higher than at any point in Virgin Money's history;
- we continued to outstrip growth in the savings market as a whole with balance growth of 12.4% compared to market growth of 6.9% over the course of 2015. We took a 3.0% market share of net inflows, up from 1.6% in 2014, and grew our market share of savings stock from 1.4% at December 2014 to 1.5% at December 2015;
- our Cash ISA performance was particularly strong in 2015, taking a 20.1% share of net inflows in the market which reflected the strong appeal of our customer proposition. This performance resulted in our Cash ISA market share increasing to 4.1% at the end of December 2015, from 3.0% at the end of 2014. We also won the Personal Finance Best Cash ISA award and a Your Money Best Cash ISA Award for the third year running;
- in March we introduced a new defined access saver product, broadening our range of variable savings products and continuing to offer competitive rates for customers; and
- our new Help to Buy ISA product was launched in December 2015 under the Government scheme which provides financial assistance to first-time buyers through a tax efficient savings product.

2015 financial highlights

- net interest income increased by 23% to £358.5 million as a result of the growth in mortgage balances and improved NIM. Combined with a modest and expected reduction in other income, our total income rose by 23% to £361.0 million;
- strong cost management produced a positive differential between 8% cost growth and 23% income growth;
- our contribution improved by 28% in 2015 reflecting strong asset growth and continued high asset quality, allied with careful pricing and cost management;
- we delivered a full year NIM of 1.52% in the mortgage and savings business. This was achieved through optimisation of mortgage product mix within our risk appetite and careful management of the cost of retail products whilst maintaining a good value offering for customers;
- our provisions represented 10% of impaired loans. In addition to provisions, which reflect the high quality of the book and low loss experience, we have a regulatory requirement to make an adjustment to capital (the excess expected loss) which amounted to a capital deduction of £35.4 million at the end of 2015; and
- risk-weighted assets at year end increased by 15% reflecting increased lending and a change to our AIRB model in June 2015 which reduced average risk weight intensity in our mortgage book.

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Financial results

Divisional results

Performance summary – Mortgages and Savings

	2015 £m	2014 £m	Change
Net interest income	**358.5**	291.0	23%
Other income	**2.5**	3.1	(19)%
Total underlying income	**361.0**	294.1	23%
Total costs	**(92.7)**	(85.7)	8%
Impairment	**(3.0)**	(1.2)	150%
Contribution	**265.3**	207.2	28%
Mortgages and savings net interest margin	**1.52%**	1.42%	10bps
Cost of risk	**0.01%**	0.01%	–

	2015 £m	2014 £m	Change
Key balance sheet items at 31 December			
Loans and advances to customers	**25,453.5**	21,887.5	16%
– of which prime residential	**21,052.6**	18,753.3	12%
– of which buy-to-let	**4,400.9**	3,134.2	40%
Customer deposits	**24,914.6**	22,164.1	12%
Total customer balances	**50,368.1**	44,051.6	14%
Risk-weighted assets	**4,284.5**	3,729.8	15%

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Divisional results

Credit Cards

We provide credit card products, primarily online, to over 700,000 customers. Our portfolio is a mix of balance transfer and retail credit cards. Our Credit Card business contributed 22% of total income in 2015.

Strategy

Our Credit Card business was previously delivered through a partnership with MBNA. In March 2015 we successfully migrated 675,000 customer accounts to our own platform. This gives us an in-house capability to issue credit cards and manage our portfolio. Our credit card manufacturing capability was developed in partnership with leading credit card systems provider TSYS.

The new platform allows us to respond to market conditions more quickly and better align our products to customer needs. We will continue our presence in the balance transfer market and further diversify our product range.

In 2014 we announced that we aimed to grow credit card balances to at least £3 billion by the end of 2018. We now aim to reach that target a year earlier by the end of 2017.

Key developments

- we have made a strong start to origination on our own platform with the number of new cards written exceeding expectations;
- we achieved a 2.5% share of the £65 billion credit card market in 2015. This represented a 0.7 percentage point increase from our 1.8% share of the £62 billion market in 2014;
- much of our effort in the earlier part of the year was dedicated to the successful migration of customer accounts to our own platform in March. The project was completed on time and within budget;
- having our own credit card capability in place has allowed us to start growing the business through simple, transparent products supported by strong risk management and analytical capability;
- we have expanded our product offering as we have sought to cater for different customer needs in the balance transfer and retail card segments; and
- as a result of our successful re-entry into the market, we ended the year with over 185,000 new customers. This represented an increase of 140,000 from the number of new customers acquired in 2014 and underlines our ability to grow on our own platform.

2015 financial highlights

- strong customer uptake of our cards led to contribution increasing by 13% to £51.2 million;
- net interest income grew by 30% to £97.6 million reflecting the growth in balances, predominantly in the second half of the year;
- other income fell as expected by 29% due to the absence of card origination commissions from MBNA in 2015 and a reduction in cash advance fees. Cash advance fees on cards within their EIR life are recognised in net interest income. This reduction was partially offset by an increase in interchange fee income due to a 41% increase in overall retail spend. This increase was driven both by strong take up of new retail card products and a 7% increase in average retail spend per active card;
- total income increased by 15% reflecting the reduction in other income partially offsetting the increase in net interest income;
- net interest margin decreased by 1.38 percentage points to 8.22% as a result of the growth in the number of front book customers;
- total costs fell 8% as we stopped paying MBNA for the servicing of customer accounts from the date of migration in March. In the first quarter we were paying MBNA for card servicing while also incurring the cost of our own platform in preparation for migration. Operating costs per average active account on our own platform in the last nine months of the year were approximately 30% lower than the comparable unit cost on the MBNA platform in the first quarter;

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Financial results

Divisional results

- the impairment charge for credit cards, gross of debt sale recoveries, increased by 46% to £34.2 million. The impairment charge, net of debt sale recoveries, increased by 87% to £27.3 million;
- this was largely due to the fact that no charged-off balances originated in 2013 were sold in that year. In 2014 charged-off balances originated in both 2013 and 2014 were sold, benefiting the 2014 impairment charge net of debt sale recoveries;
- the cost of risk for credit cards gross of debt sale recoveries was broadly flat at 2.50%. Net of debt sale recoveries, the cost of risk for credit cards increased by 49bps to 2.00% in 2015, from 1.51% in 2014;
- loans and advances to customers increased by 44% to £1,578.7 million; and
- risk-weighted assets in the division, including both credit risk weighted assets and operational risk weighted assets increased by 37% mainly due to the increase in loans and advances on the balance sheet.

Performance summary – Credit Cards

	2015 £m	2014 £m	Change
Net interest income	**97.6**	75.1	30%
Other income	**18.0**	25.2	(29)%
Total income	**115.6**	100.3	15%
Total costs	**(37.1)**	(40.5)	(8)%
Gross impairment charge	**(34.2)**	(23.5)	46%
Debt sale recoveries	**6.9**	8.9	(22)%
Net impairment charge	**(27.3)**	(14.6)	87%
Contribution	**51.2**	45.2	13%
Credit cards net interest margin	**8.22%**	9.60%	(138)bps
Cost of risk (gross of recoveries)	**2.50%**	2.43%	7bps
Cost of risk (net of recoveries)	**2.00%**	1.51%	49bps

	2015 £m	2014 £m	Change %
Key balance sheet items at 31 December			
Loans and advances to customers	**1,578.7**	1,098.2	44%
Total customer balances	**1,578.7**	1,098.2	44%
Risk-weighted assets	**1,334.7**	973.2	37%

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Divisional results

Current Accounts, Insurance and Investments

This division manages and develops our current accounts, insurance and investment offerings. We work with a number of partners to deliver these products.

This part of our business contributed 7% of total income in 2015.

Strategy

Our insurance and investment strategy is based on a partnership model. We seek partners who share our commitment to straightforward and transparent products. We leverage their capabilities with our brand and marketing expertise to access profitable sectors whilst moderating financial risk.

We have commenced a Personal Current Account (PCA) feasibility study with a view to defining our entry into the broader PCA market.

Key developments

- we completed the national roll out of the Virgin Essential Current Account to customers in the first quarter of 2015. The Virgin Essential Current Account aligns with the Government initiative on Basic Bank Accounts and has been well received by consumers with the number of accounts opened ahead of expectations;
- our potential to grow profitably at scale in current accounts at present is limited by the structure of the UK current account market, including the low level of switching and the predominance of free-if-in-credit banking. Our feasibility study will consider these issues;
- we launched our simple, transparent life insurance product in partnership with Friends Life in March 2015;
- we launched the sale of general insurance in the fourth quarter of 2015 under our long-term strategic partnership with Ageas;
- we launched three new funds during the first half of the year, increasing the number of passively managed funds in our range to five. The new funds provide our customers with more choice and give us the opportunity to grow our funds under management;
- we launched an international money transfer service in partnership with World First and a travel money service in partnership with Travelex in the second half of 2015; and
- following these launches, the foundations for the growth of the Insurance and Investments businesses are largely in place.

2015 financial highlights

- our funds under management stood at £3.0 billion at 31 December 2015 helping to drive a 9% increase in investment income;
- the number of new Stocks & Shares ISA applications declined compared with 2014 reflecting the new flexibility for customers to make full use of their tax free allowance to save in cash;
- our pension sales continued to perform well;
- our insurance income in 2015 grew 13% reflecting our expanded product range;
- our current account balances grew by 14% in the year to £230.3 million;
- attributable expenses increased by 24% due to the strengthening of the management team and the restructuring of a commercial contract with a corporate partner; and
- risk-weighted assets are held against operational risk in the business unit. Operational risk-weighted assets are measured using income generated by the unit in the preceding three years. This led to an increase of 9% year-on-year.

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Financial results

Divisional results

Performance summary – Current Accounts, Insurance and Investments

	2015 £m	2014 £m	Change %
Investments	31.6	29.0	9%
Insurance and other	5.0	3.8	32%
Total income	36.6	32.8	12%
Total costs	(16.7)	(13.5)	24%
Contribution	19.9	19.3	3%

	2014 £m	2013 £m	Change %
Key balance sheet items at 31 December			
Loans and advances to customers	0.1	0.1	–
Customer deposits	230.3	201.6	14%
Total customer balances	230.4	201.7	14%
Risk-weighted assets	51.6	47.2	9%

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Divisional results

Central Functions

Our Central Functions division provides shared support services to each of our business lines. These services include Information Technology and Property together with functions such as Risk, Finance, Treasury, Human Resources and the Group's Executive. It is not our policy to allocate the cost of these shared functions to each business line.

Our divisional view of the business allocates directly attributable costs to the main income lines, with the remainder of overheads in central functions.

This part of our business contributed 2% of total income in 2015.

Key developments

- we invested over £40 million to improve our capability, fully aligned with our strategy to grow the business. We delivered multiple key initiatives in 2015, including the migration and launch of our new Credit Card and the launch of the Essential Current Account, Life Insurance, Home & Motor Insurance, Travel Money and International Money Transfer products. We also supported the launch of the Virgin Money Foundation;
- during the year we successfully piloted and rolled out an enhanced mortgage processing approach, delivering further improvements to the speed of making mortgage offers to customers. A Day 1 underwriting decision, alongside our continued focus on quality, has given us a competitive advantage in the market place;
- we continued to build upon our digital and mobile capability which will serve to improve our customers' journeys whether they apply for our products in store, over the telephone, online or via an intermediary; and
- we continued to invest in our security programme in order to safeguard our business. This delivered enhanced network security, web protection and a strengthening of our processes around the prevention of data loss. In addition, a Chief Security Officer was appointed bringing us extensive experience in the field.

2015 financial highlights

- interest income and expense incurred from Treasury funding and liquidity operations is allocated to the divisions;
- other income is primarily due to gains on the sale of investment securities from within the Treasury portfolio;
- the fair value gain on FTSE 100 equity options reduced by 90% to £0.2 million as the options had been struck to protect against a weaker FTSE 100 performance than was the case for the year ending 31 December 2015;
- a £6.3 million increase in depreciation and amortisation stemmed from capital expenditure in prior years from our annual investment spend, as we continued to invest in our future;
- stripping out the cost of increased depreciation, amortisation and continued investment, the cost of running the division was broadly flat; and
- costs also included the opening of our new lounge on Haymarket in London during the year.

The financial metrics in this section are presented on an underlying basis unless labelled as statutory.

Financial results

Divisional results

Performance summary – Central Functions

	2015 £m	2014 £m	Change
Fair value gain on FTSE 100 equity options	**0.2**	2.0	(90)%
Other income	**9.7**	9.0	8%
Total income	**9.9**	11.0	(10)%
Total costs	**(186.0)**	(177.9)	5%
Loss	**(176.1)**	(166.9)	6%

	2015 £m	2014 £m	Change %
Key balance sheet items at 31 December			
Risk-weighted assets	**439.6**	410.4	7%

Governance

Virgin Money Lounge, Glasgow

Board of Directors

Chairman

Glen Moreno (72)

Joined the Board in January 2015 and became Chairman in May 2015

Chair of the Nomination Committee

Skills and experience:

Glen has over 40 years' experience in business and finance gained from senior positions in a wide range of industries. Glen's deep financial services knowledge and experience, leadership qualities and standing with key stakeholders made him the unanimous choice of the Board to become Chairman of Virgin Money.

External appointments:

- Non-Executive Director of Fidelity International Limited.

Former key appointments:

- Chairman of Pearson plc (2005 to 2015);
- Deputy Chairman of the Financial Reporting Council (FRC) (2010 to 2014);
- Senior Independent Director at Lloyds Banking Group plc and Deputy Chairman in the latter part of his tenure (2010 to 2012);
- Acting Chairman of UK Financial Investments Limited (2009);
- Senior Independent Director at Man Group plc (2001 to 2009); and
- Chief Executive of Fidelity International Limited (1987 to 1991).

Senior Independent Director (SID)

Norman McLuskie (71)

Joined the Board in January 2010

Chair of the Audit Committee

Member of the Nomination Committee, the Board Risk Committee and the Remuneration Committee

Skills and experience:

Norman has over 30 years of experience in financial services having served in a number of senior positions at Royal Bank of Scotland Group (RBS). He is a chartered accountant and has significant financial experience in the UK listed environment and so is well placed to carry out the SID and Chair of the Audit Committee roles for Virgin Money. Norman is a fellow of the Chartered Institute of Bankers in Scotland.

External appointments:

- None.

Former key appointments:

- Non-Executive Director of RBS Insurance (2004 to 2010);
- Chairman of MasterCard Europe (2004 to 2007);
- Deputy Chief Executive at RBS (1998 to 2000); and
- Director of RBS (1992 to 2004).

Independent Non-Executive Directors

Colin Keogh (62)

Joined the Board in January 2010

Chair of the Board Risk Committee

Member of the Audit Committee and the Nomination Committee

Skills and experience:

Colin has spent his entire career in financial services, principally at Close Brothers where he worked for 24 years and held a number of senior management and board positions. His deep understanding of risk management, underpinned by his knowledge of banking operations, is invaluable in his role as Chair of the Board Risk Committee. Colin is a barrister of law.

External appointments:

- Senior Independent Director and Chair of the Remuneration Committee of Hiscox Limited; and
- Chairman of Premium Credit Limited.

Former key appointments:

- Non-Executive Director of Brait SE, a specialist investment company listed in Johannesburg and Luxembourg (2010 to 2016);
- Non-Executive Director of New World Resources plc, a London listed mining company (2014 to 2015);
- Non-Executive Director of Emerald Plantation Group, Emerald Plantation Holdings Limited and Greenheart Group Limited (2013 to 2015); and
- Group Chief Executive of Close Brothers Group plc (2002 to 2009).

Marilyn H Spearing (61)

Joined the Board in January 2014

Chair of the Remuneration Committee

Member of the Audit Committee, the Board Risk Committee and the Nomination Committee

Skills and experience:

Marilyn has extensive financial services experience, particularly in managing organisational, operational and structural change. Marilyn became Chair of the Remuneration Committee in January 2016. Her strong understanding of remuneration and risk governance makes her ideal for that role. During her executive career, Marilyn also specialised in payments, cash management and related technology platforms.

External appointments:

- None.

Former key appointments:

- Global Head of Trade Finance and Cash Management at Deutsche Bank AG (2006 to 2012);
- Global Head of Payments and Cash Management at HSBC (1995 to 2006); and
- Positions on the Boards of SWIFT (UK) Limited (2005 to 2011) and VOCA Limited (2000 to 2005).

Board of Directors

Independent Non-Executive Directors

Geeta Gopalan (51)

Joined the Board in June 2015

Member of the Audit Committee, the Board Risk Committee, the Remuneration Committee and the Nomination Committee

Skills and experience:

Geeta's broad experience and knowledge of the financial services industry, particularly around payments and digital innovation, is invaluable to Virgin Money as the business develops new products and digital capability. She also has extensive experience of boards in a wide range of sectors. Geeta is a chartered accountant.

External appointments:

- Independent Non-Executive Director of Vocalink Holdings Limited and its subsidiary Advanced Payment Technology Limited; and
- Non-Executive Member and Vice Chair of the England Committee of the Big Lottery Fund.

Former key appointments:

- Chair of Monitise Europe, the AIM listed mobile payments company (2009 to 2010);
- Director of Payment Services with HBOS plc (2005 to 2007); and
- Managing Director, UK Retail Bank and Business Development Head EME at Citigroup (2002 to 2005).

Non-Executive Directors

Gordon McCallum (55)

Joined the Board in January 1998

Member of the Nomination Committee

Skills and experience:

Gordon has extensive board, financial and general management experience across a range of sectors including media, telecommunications, financial services and renewables. He brings a breadth of experience gained from leading the strategic development of the Virgin Group from 1998 to 2012.

External appointments:

- Virgin-nominated Non-Executive Director at Virgin Atlantic Limited and Virgin Holidays Limited;
- Serves in a Non-Executive capacity on the boards of a number of non-Virgin companies. These include John Swire & Sons Limited and Hunter Boot Limited in the UK and the Advisory Board of Aldo Group in Canada; and
- Senior advisory role to private equity firm, Searchlight Capital.

Former key appointments:

- Various senior executive positions at the Virgin Group (1998 to 2015); and
- Management consultant at McKinsey & Co and an investment banker at Baring Brothers in London and Asia.

Non-Executive Directors

Patrick McCall (51)

Joined the Board in June 2012

Skills and experience:

Patrick has an extensive background in the finance, capital markets, retail, travel and healthcare sectors. He has significant experience at board level, as an Executive, Non-Executive and Chairman. He is a strong advocate for customers, the Virgin brand and the application of new products and technology, all of which are aligned with Virgin Money's strategy. He also has considerable experience in complex project delivery and material outsourcing.

External appointments:

- Senior Managing Director of the Virgin Group; and
- Virgin nominated Non-Executive Director at Virgin Active, Virgin Rail Group, Virgin Trains East Coast, Virgin Galactic and OneWeb.

Former key appointments:

- Investment banker at SG Warburg (1987 to 1997).

Executive Director and Chief Executive

Jayne-Anne Gadhia, CBE (54)

Joined the Board in March 2007

Skills and experience:

Jayne-Anne has significant finance and banking experience, built up over a period of almost 30 years. Jayne-Anne's commitment to building Britain's best loved bank, along with her proven ability to build businesses and lead strong management teams, brings significant value to all stakeholders of Virgin Money. Jayne-Anne is a chartered accountant.

External appointments:

- Chair of Scottish Business in the Community[1];
- Non-Executive Director of Business in the Community[1];
- A number of advisory roles: Financial Services Advisory Board, Prime Minister's Business Advisory Group and FCA Practitioner Panel Advisory Group; and
- Leading the government's "Harnessing Talents of Women in Financial Services Review".

Former key appointments:

- RBS Retail Executive Board where she was responsible for the RBS Group's mortgage business (2001 to 2007);
- Became one of the founders of Virgin Direct before launching the market-leading Virgin One account in 1998 (1995 to 2001); and
- Marketing director of Norwich Union's Unit Trust business (1987 to 1995).

1 Body not for commercial purposes.

Board of Directors

Company Secretary

Katie Marshall (38)

Appointed September 2013

Skills and experience:

A qualified solicitor, Katie joined Virgin Money in 2009, following ten years as a corporate lawyer at Eversheds LLP. Katie has experience of a wide range of corporate transactions and governance matters. Katie was appointed Company Secretary in September 2013.

Virgin Money Executive

Board Member

Jayne-Anne Gadhia, CBE (54)
Chief Executive

Jayne-Anne joined the Board in March 2007 as Chief Executive.

Further details can be found on page 77.

Non Board Members

Dave Dyer (59)
Chief Financial Officer

Dave is an accountant and qualified whilst employed with Citibank. Following his MBA, Dave worked at Touche Ross, before joining Somerfield Supermarkets as commercial director, moving to RBS in 1994. At RBS, Dave played a central role in the creation of the Virgin One account and in 1999 became its Finance Director. In 2006, Dave became Finance Director, mortgages within RBS. In 2007, Dave joined Virgin Money as Chief Financial Officer (CFO) and subsequently became Strategy Director in 2009. Dave was reappointed to the role of CFO in September 2015. Dave will hold this position until he hands over responsibilities to the CFO designate, Peter Bole.

Marian Martin (48)
Chief Risk Officer

Marian is a chartered accountant and qualified with Ernst and Young. She joined the Britannia Building Society where she was internal audit manager, before spending four years at the Britannic Group where she was head of group audit and risk. Marian joined RBS in 2004 and served as Risk Director of the RBS Group's consumer finance businesses, the mortgage business and then Tesco Personal Finance. Marian joined Virgin Money in 2007.

Matt Elliott (42)
HR Director

Matt's early career was at RBS, where he worked on HR policy and employment issues, before supporting the HR transformation programme following the acquisition of NatWest. Matt held senior HR roles in several RBS operating businesses including the Consumer Finance division and Tesco Personal Finance. In 2007, Matt moved to BP as senior manager for corporate and functions before becoming HR Vice President for BP in North Africa. He joined Virgin Money in 2011.

Michele Greene (50)
Director of Strategic Development

Michele is a chartered accountant and qualified with KPMG. She spent three years at Credit Lyonnais as a financial accountant before joining Goldman Sachs as group accountant. Michele spent over 15 years at MBNA, most recently as CFO, where she was a member of the board and closely involved in setting the strategic direction of the business. Michele joined Virgin Money in October 2013.

Virgin Money Executive

Non Board Members

Richard Hemsley (51)
Chief Banking Officer

Richard is a qualified banker and has over 30 years' experience across the industry within the UK. He joined NatWest in 1983 working across retail and corporate banking, fund management and major change programmes. After the acquisition of NatWest by RBS in 2000, he worked in operations becoming the group Chief Operations Officer (COO) in 2008, leading a global team of over 40,000 people, and then COO of transaction and international banking in 2011. Immediately prior to joining Virgin Money in January 2015, Richard was Managing Director of Lombard, the UK's largest asset finance business.

Andrew Emuss (46)
General Counsel

Andrew qualified as a solicitor in 1996. He started his career at Clifford Chance, qualifying as a corporate lawyer, and has spent almost 20 years leading corporate and capital markets deals. He spent over ten years at Nomura and served as its head of corporate development for EMEA, executing strategic deals. Andrew joined Virgin Money in June 2014.

Caroline Marsh (52)
Director of Culture

Caroline has over 29 years' experience in banking. Her early career was at Barclays where she spent 12 years in management roles. In 1999, she joined Virgin One as sales director. Following the acquisition of Virgin One by RBS in 2001, Caroline became Sales and Operations Director for the RBS consumer finance business, before leading the bank's intermediary mortgage business. Caroline returned to Virgin Money in 2007 as Sales Director and has led the cultural agenda for the Virgin Money business since the acquisition of Northern Rock in 2012.

Corporate Governance Report

"Our customer-focused strategy, underpinned by our culture and strong corporate governance, provides the foundation that makes Virgin Money an attractive investment."

Dear Shareholders

I am pleased to present our Corporate Governance Report for 2015. This report explains how the Group applies the principles of good corporate governance, in particular those laid down in the 2014 edition of the Financial Reporting Council's (FRC) UK Corporate Governance Code (Code)[1].

I am pleased to report that during the year the Board and its Committees met their objectives and carried out their responsibilities effectively. Further detail can be found on pages 92 to 93 and in the Board Committee Reports on pages 96 to 110.

Set out below are the principal corporate governance matters considered in 2015.

Chairman succession

I was appointed to the Board as an Independent Non-Executive Director on 1 January 2015. I succeeded Sir David Clementi as Chairman on 21 May 2015.

In this first full year following our listing on the London Stock Exchange, I have taken the opportunity to review the Group's governance arrangements and undertake a robust, externally-facilitated Board Effectiveness Evaluation exercise. I am confident that the resulting recommendations, when fully implemented, will strengthen Board effectiveness and will position the Board well to achieve our strategic objectives. Further detail on both reviews can be found in this report.

Board composition

There have been a number of changes to the Board.

Geeta Gopalan was appointed as an Independent Non-Executive Director in June. Geeta's broad experience and knowledge of the financial services industry, including digital innovation, will be invaluable to us as we continue to grow the business. In addition, Marilyn Spearing became Chair of the Remuneration Committee, following Olivia Dickson's retirement from the Board on 31 December 2015.

As announced in January 2016, Peter Bole will join us as Chief Financial Officer (CFO) in 2017, following which he will be appointed as an Executive Director. This appointment followed Lee Rochford's decision to leave the business in August 2015. More information on the Board's approach to the recruitment of Directors and the skills and experience of Peter and Geeta is set out on pages 97 and 98.

James B Lockhart III, WL Ross' (WLR) nominee director, also stepped down as a Non-Executive Director in September, as a result of WLR, previously a controlling shareholder of the Group (for the purposes of the Listing Rules), reducing its shareholding from 33.5 per cent to 12.0 per cent.

We continue to strive for a balanced Board and remain committed to increasing diversity. We therefore aim to appoint an additional Independent Non-Executive Director in 2016 as part of our medium-term succession planning.

Culture

The Board should articulate and promote a culture of risk awareness and ethical behaviour for the entire organisation to follow in pursuit of its business goals. The Non-Executive Directors play a key role in holding management to account for embedding and maintaining this culture.

At Virgin Money we are proud of a culture that sustains our ambition to make 'Everyone Better Off' and believe our culture cannot be readily and credibly replicated in the UK banking sector. Our culture provides the foundation for the Group's strategy and differentiated approach to banking.

1 The Code can be accessed at frc.org.uk.

Corporate Governance Report

Board effectiveness

The Board Effectiveness Evaluation was undertaken in the second half of 2015 by Boardroom Review Limited. It offered an independent view of the Board and Committees' effectiveness and has provided the Board with a roadmap for its development. It also illustrated how the Directors can optimise their contribution to the success of the Group, both individually and collectively, and add value by building on existing strengths, agreeing the challenges ahead and preparing for the future. Further detail is contained on pages 92 to 93.

I would like to thank Dr Tracy Long of Boardroom Review Limited for her thorough and insightful review and my fellow Board members and Executive for the time and support given by them to the evaluation.

Regulatory governance changes and developments

We welcome the implementation this month of the Senior Managers and Certification Regimes and new Conduct Rules and the clarity they will bring to lines of responsibility and accountability.

We view the regimes and their application as consistent with the principle of collective decision-making which underpins good Board decision-making.

We continue to participate in regulatory consultations on corporate governance and to work with the relevant authorities on the introduction of regulations connected to the Financial Services (Banking Reform) Act 2013. The Act will result in the ring-fencing of retail and commercial operations to separate them from investment banking activities. Given that we are a UK focused retail bank, we expect our entire business will be within the ring-fence when it comes into effect at the beginning of 2019.

External auditor

During the year the Board, on the recommendation of the Audit Committee, appointed PricewaterhouseCoopers LLP (PwC) as external auditor for the Group's 2016 audit, following a formal competitive tender overseen by the Audit Committee. This appointment will be put to shareholders for approval in May at the 2016 Annual General Meeting (AGM).

I would like to take the opportunity to thank KPMG LLP for the insight they have brought and the value that they have added to the business during their tenure. We expect an orderly transition and look forward to working with PwC in the future.

Looking ahead

I am delighted to welcome the increasing number of retail and institutional shareholders investing in Virgin Money and look forward to engaging with our shareholders over the course of 2016.

Finally, I would like to thank each of the Directors for their commitment during 2015 and for their support during the first nine months of my Chairmanship. We are very well-placed to make the most of the opportunities that exist and I look forward to building on what we have achieved so far.

Glen Moreno
Chairman

1 March 2016

The Board, its members and additional support

Purpose and responsibilities

The Group is led by a Board comprising a Non-Executive Chairman, Non-Executive Directors (the majority of whom are independent) and an Executive Director. The Board is collectively responsible for the long-term success of Virgin Money. It achieves this by setting the strategy and overseeing delivery against it. It establishes the culture, values and standards of the Group, effectively managing risk, monitoring financial performance and reporting, and ensuring that appropriate and effective succession planning arrangements and remuneration policies are in place.

The role of the Directors

Set out below are the roles of the Chairman and other Board members. There is a clear division of responsibility at the head of the Group. The Chairman has overall responsibility for the leadership of the Board while the Chief Executive manages and leads the business.

Chairman

Glen Moreno joined the Board in January 2015 as Chairman designate and became Chairman on 21 May 2015, following the retirement of Sir David Clementi.

The Chairman:

– has overall responsibility for the leadership of the Board and promotion of the highest standards of corporate governance;
– has responsibility for leading the development of the Group's culture by the Board as a whole;
– sets the Board's agenda to ensure that the Board devotes its time and attention to the right matters;
– builds an effective and complementary Board;
– plans succession in Board appointments in conjunction with the Nomination Committee;
– ensures the Directors receive timely and relevant information and are kept advised of developments; and
– ensures effective communication with shareholders.

Chief Executive

Jayne-Anne Gadhia was appointed Chief Executive in March 2007.

The Chief Executive:

– manages the Group on a day-to-day basis and in accordance with the strategy and long-term objectives approved by the Board;
– with the exception of those matters reserved to the Board, makes decisions on all areas affecting the operations, performance and strategy of the Group's business;
– provides leadership and direction to senior management;
– co-ordinates all activities to implement the Group's strategy and for managing the business in accordance with the Group's risk appetite and business plan set by the Board; and
– has responsibility for overseeing the adoption of the Group's culture in the day-to-day management of the Group.

Non-Executive Directors

The Non-Executive Directors are listed on pages 74 to 77.

Non-Executive Directors:

– challenge constructively;
– help develop and set the Group's strategy;
– participate actively in the decision-making process of the Board;
– scrutinise the performance of management in meeting agreed goals and objectives;
– provide entrepreneurial leadership of the Group within a framework of prudent effective controls;
– satisfy themselves as to the integrity of financial information and systems of risk management; and
– determine appropriate levels of remuneration of Executive Directors via the Remuneration Committee.

Senior Independent Director

Norman McLuskie was appointed Senior Independent Director in January 2010.

The Senior Independent Director:

– helps resolve shareholders' concerns;
– acts as a sounding board for the Chairman and Chief Executive on Board and shareholder matters;
– is a conduit, as required, for the views of other Non-Executive Directors on the performance of the Chairman;
– is available to shareholders if they have concerns which contact through the normal channels has failed to resolve or for which such contact is inappropriate;
– if required, attends meetings with major shareholders and financial analysts to understand issues and concerns; and
– conducts the Chairman's annual performance appraisal.

Corporate Governance Report

The role of the Chief Financial Officer (CFO)

The CFO is responsible for the financial management of the Group and day-to-day management of the balance sheet. The CFO ensures that the Group meets statutory reporting obligations, ensures the delivery of regulatory capital and liquidity requirements and identifies opportunities to improve the profit and loss performance of the business within the agreed risk appetite. The CFO also maintains appropriate cash resources and projections and ensures compliance with the terms of external debt facilities.

The current CFO is not a Board member but is invited to Board meetings to provide specialist support as appropriate.

In January 2016, the Group announced the agreed appointment of Peter Bole as CFO. It is expected Peter will join Virgin Money as CFO in 2017, following which he will be appointed as an Executive Director. Dave Dyer will remain as CFO, providing support to the Board, until he hands over responsibilities to Peter. He is not an Executive Director. Please see page 98 of the Nomination Committee Report for further details.

The role of the Company Secretary

The Company Secretary is accountable to the Board. The Company Secretary provides comprehensive practical support to the Directors, both as individuals and as a collective, with particular emphasis on supporting the Non-Executive Directors in maintaining appropriate standards of probity and corporate governance. The Company Secretary is also responsible for facilitating communications with shareholders, as appropriate, and ensuring due regard is paid to their interests. All Directors, including Non-Executive Directors, have access to the advice and services of the Company Secretary in relation to the discharge of their duties.

Access to advice

The Group also provides access, at its own expense, to the services of independent professional advisers in order to assist the Directors, in particular Non-Executive Directors, in their roles whenever this is deemed necessary. Board Committees are also provided with sufficient resources to undertake their duties.

Authority and delegation

Corporate governance framework

The Group's corporate governance framework, which is reviewed annually by the Board, comprises the Board authority and the delegated executive authority.

Board authority

The Board authority sets out the matters reserved to the Board. This includes decisions concerning the strategy and long-term objectives of the Group, capital and financial budgets, significant contracts and transactions and various statutory and regulatory approvals. The approval of the remuneration policy, risk appetite and risk management framework are also reserved to the Board. The Board authority delegates responsibility for day-to-day management of the business to the Chief Executive and sets out the basis for delegation of authorities from the Board to Board Committees.

Further details of Board reserved matters can be found at virginmoney.com/virgin/investor-relations.

The following table provides an overview of the key matters considered by the Board in 2015:

Strategy and budget	Structure, capital and transactions	Finance, statutory and regulatory requirements
The Board: – approved an update to the Group's strategy and long-term objectives; – approved an update to the three-year financial plan and the 2016 operating plan and budget; – reviewed delivery against plan; and – reviewed strategic proposals and operational issues.	The Board: – considered acquisition opportunities; – determined the funding strategy to optimise funding costs, extend tenor and ensure appropriate diversification in the funding base; – approved the first issue under the Medium Term Note (MTN) programme and further Residential Mortgage Backed Securities (RMBS) programmes; and – approved changes to the capital structure, including additional listings to satisfy share vestings.	The Board: – approved the annual report and interim accounts and significant accounting changes; – approved the shareholder notice of AGM; – approved the interim dividend and proposed the final dividend; and – considered regulatory changes to be introduced by, amongst others, the Banking Reform Act including retail ring-fencing, the EU Mortgage Credit Directive and significant developments in regulatory capital and liquidity requirements.
Remuneration	**Risk management**	**Governance**
The Board: – approved the Directors' remuneration policy and the overall remuneration policy and philosophy of the Group; – approved the remuneration and structure of NED fees for 2015 and 2016; and – approved the remuneration policy measures for bonuses and the Long Term Incentive Plan (LTIP).	The Board: – approved the Group's risk appetite and risk management framework; – monitored the Group's aggregate risk exposures, risk/return and emerging risks; – reviewed the effectiveness of the Group's risk management and internal control systems; – approved Recovery and Resolution Plans updated to reflect the requirements of the EU Bank Recovery and Resolution Directive; and – conducted deep dives into cybercrime and information security.	The Board: – determined the Board and Committee structures, size and composition; – facilitated a Board Effectiveness Evaluation; – carried out an annual review of the corporate governance framework, Board Committee terms of reference and key Group policies; – considered the independence of Non-Executive Directors; – appointed a new Chairman and new Non-Executive Director to the Board; and – considered Board and Executive (including CFO) succession planning and appointment.

Board Strategy Review

During the year, the Board spent considerable time discussing, debating and devising the business strategy for the next three years. The aim of the strategy is to build on the Group's unique position as a strong, low risk retail bank, unburdened by legacy conduct issues. This was the first strategic review undertaken since listing on the London Stock Exchange and the Board remains committed to maintaining the Group's growth momentum, continuing to build a high-quality balance sheet and generating sustainable and strong shareholder returns within its prudent risk appetite. The strategic review considered and incorporated the three-year financial plan, the 2016 operating plan (including culture, the development of the existing business and the transformational change agenda) and the external environment.

The potential for consolidation in UK retail banking, the requirement to grow non-interest income and deepen customer relationships, digital transformation, conducting a Personal Current Account (PCA) feasibility study with a view to defining entry into a broader PCA market, and the development of a Small Medium Enterprises (SME) strategy, were all discussed in detail. Risk oversight and risk appetite, together with a review of organisational capability and structure, also featured.

Together, these issues were considered very carefully by the Board to ensure the business is able to continue delivering sustainable success for all stakeholders.

Outcomes from discussions held by other Committees were also assessed and considered. For example, the Board Risk Committee considered risk appetite amendments required to support the strategic plan. This included those driven by regulatory or policy changes and a reassessment of business requirements. In addition, the Nomination and Remuneration Committee provided oversight regarding organisational structure, capability changes and succession matters. As a result, the Executive was strengthened to support the continued growth of the business.

Corporate Governance Report

Delegated executive authority

The Chief Executive, through the delegated executive authority, delegates aspects of her own authority, as permitted, to members of the Executive.

On a daily basis, the Executive discuss business performance and issues within the business. The majority of the Executive Committees meet to scrutinise key business matters on a monthly basis. Certain Executive Committees, such as the Disclosure Committee, may meet more regularly and as required.

The Internal Audit Director and the Company Secretary, or their representatives, attend all Executive Committee meetings to ensure that there is appropriate internal audit oversight and that the highest standards of corporate governance are maintained, including the escalation of matters to the Board and its Committees. Other representatives from the business attend as necessary and appropriate.

Virgin Money Holdings (UK) plc
Board of Directors

Nomination Committee
Keeps under review the leadership needs of the Group, including an annual review of the structure, size and composition of the Board. Develops and maintains a formal, rigorous and transparent procedure for making appointments to the Board and reviewing succession planning at Board and senior Executive level.

Audit Committee
Monitors and reviews the Group's financial reporting arrangments, the adequacy and effectiveness of the internal controls and risk management systems, including whistle-blowing and the work of the internal and external audit processes. Manages all relationships with the external auditor.

Board Risk Committee
Monitors the Group's compliance with the Board's approved risk appetite, risk management framework and risk culture.

Remuneration Committee
Recommends an overall remuneration policy and philosophy that is aligned with the long-term interests of the Group, business operations, risk appetite and values. Determines the framework and policy on terms of engagement (including remuneration) of the Chairman, Board members and senior management.

Chief Executive – Jayne-Anne Gadhia
Responsible for managing the business of the Group in accordance with the strategy and long-term objectives approved by the Board.

Executive – and Executive Committees
Please see pages 79 and 80 for a list of the Executive and page 145 for the key Executive Committees.

The role of the Board Committees

The Board is supported by its Committees which make recommendations to the Board on matters delegated to them, in particular in relation to internal control, risk management, financial reporting, governance, succession planning and remuneration matters. This enables the Board to spend a greater proportion of its time on strategic, forward looking agenda items. The current Board Committees are set out above.

Each Board Committee, other than the Nomination Committee comprises solely Independent Non-Executive Directors. The Nomination Committee comprises all the Independent Non-Executive Directors and one Non-Executive Director, Gordon McCallum, who is the director nominated by the controlling shareholder, Virgin Group Holdings Limited (Virgin) in accordance with the relationship agreement between the Group and Virgin.

Each Board Committee is chaired by an experienced Non-Executive Director who reports to the Board on the activities of the Board Committee at each Board meeting. Information on the membership, role and activities of each of the Board Committees can be found on pages 96 to 110. The terms of reference for each of the Committees are available on the Virgin Money website (virginmoney.com/virgin/investor-relations).

Governance review

During 2015, the Group conducted a review of its governance framework and processes. The review was aimed at enhancing governance structures and enabling more focused discussion regarding strategic matters, the external environment and emerging risks. The forthcoming Senior Managers and Certification Regimes were also considered as part of the review.

From a Board perspective, as a result of the review, the Group has reduced the frequency of Board and Committee meetings to drive efficiency and moved from eleven to eight scheduled Boards per year. Board meetings are now longer in duration and designed for detailed discussion on strategic and operational matters and emerging issues. In addition, the quality of Board packs were improved with an emphasis on the provision of timely, accurate and concise information to Directors, to support effective decision making. The Group has also consolidated the Board Risk Committee and Balance Sheet Committee into a single Board Risk Committee (further details are set out in the Board Risk Committee Report on page 105).

The review has also led to a streamlining and consolidation of the responsibilities of certain Executive Committees to embrace the principles of effectiveness, accountability, simplification and empowerment. The Group will continue to refine its governance framework to ensure it remains appropriate as the Group evolves.

Subsidiary governance

Regulated Entities

The Group's business is primarily conducted through Virgin Money plc (the Bank) which is regulated by the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA). The Bank is focused primarily on providing residential mortgages, savings and credit cards. It also offers a market-leading Basic Bank Account, the Essential Current Account.

The Bank Board largely replicates that of the Board, save that Gordon McCallum and Patrick McCall (the two non-independent Non-Executive Directors) are not members and the Chief Risk Officer is an additional Executive Director of the Bank Board.

The main Board Committees are replicated at the Bank level with the exception of the Nomination and Remuneration Committees that operate at the Group Board level only and consider appointments, succession and remuneration matters on a Group-wide basis.

The Group's investments, pensions and insurance business is conducted through the Company's subsidiaries, Virgin Money Unit Trust Managers Limited (VMUTM) and Virgin Money Personal Financial Service Limited (VMPFS). VMUTM and VMPFS are regulated by the FCA.

VMUTM's principal activities are the sale and management of authorised pensions and unit trusts.

VMPFS's principal activities are the provision of Stock and Shares Individual Savings Accounts (ISAs) and the marketing and distribution of general insurance and life insurance policies in the UK.

The boards of VMUTM and VMPFS include certain members of the Executive.

Other Entities

Virgin Money Giving (VMG) is a not-for-profit company within the Group and the vehicle for Virgin Money's charity fundraising and donations website. VMG has two independent non-executive directors on its board.

In August 2015, Virgin Money launched the Virgin Money Foundation (Foundation). The Foundation will promote the sustainable regeneration of economically and socially deprived communities in the UK. The board of the Foundation is made up, in the most part, of independent Trustees. Further details on the Foundation are contained on page 42.

To help manage the legal, regulatory and reputational risks associated with the Group's subsidiary entities, the Group requires that subsidiary Boards operate in accordance with the governance standards set out in the Virgin Money High Level Controls Manual, approved by the Board.

Corporate Governance Report

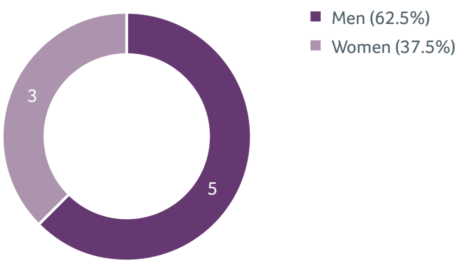
Board composition

Board size

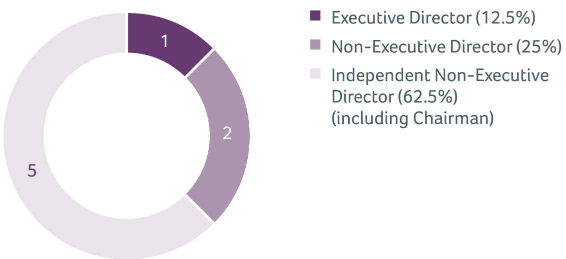
The Board should be of sufficient size and composition to reflect a broad range of views and perspectives whilst allowing all Directors to participate effectively in meetings. The Board includes a sufficient number and quality of Independent Non-Executive Directors who, between them, have sufficient breadth of understanding of the Group's activities to enable them to provide effective challenge to the Executive. The Board currently comprises one Executive Director, six Non-Executive Directors, four of whom are considered to be independent and the Chairman, who was independent on appointment.

Further details on independence and succession planning are set out in the Nomination Committee Report at pages 97 and 98.

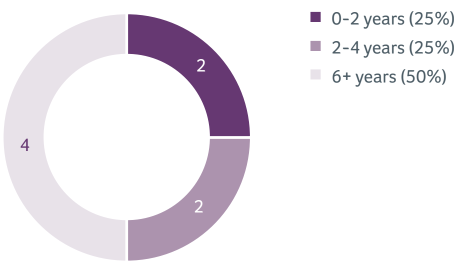
Board composition by gender



Board composition by role



Board composition by tenure



Data correct as at 1 March 2016.

Board Appointments

The chart below sets out the changes to the Board's membership in 2015. The appointment of new Directors to the Board follows a formal, rigorous and transparent procedure.

Board Changes in 2015

Total number of Directors

More information on the Board composition and the appointment process is set out in the Nomination Committee Report on pages 97 to 98.

Executive Director service agreement and Non-Executive Director terms of appointment

The Chairman and Non-Executive Directors are appointed for a specified term subject to annual re-election by shareholders. Non-Executive Directors may have their appointment terminated in accordance with the Articles of Association of the Company (Articles), their letters of appointment or statute at any time without compensation.

The Chief Executive is able to terminate her appointment by giving twelve months' notice. The Chairman has a six months' notice period. The Non-Executive Directors' letters of appointment, and the service agreement of the Executive Director, are available for inspection by shareholders at Virgin Money's registered office.

Election and re-election

All Directors appointed to the Board since the 2015 AGM and up to the date of this report will stand for election at the 2016 AGM. All other Directors will retire and those wishing to serve again will stand for re-election by shareholders at the 2016 AGM. Biographies for each of the current Directors are set out on pages 74 to 77.

As a "controlling shareholder" of the Group, Virgin will be entitled to vote on the ordinary resolutions at the AGM for the re-election of the Independent Non-Executive Directors. However, each resolution relating to the re-election of the Independent Non-Executive Directors will also require, for the purposes of the Listing Rules, approval by a majority of the votes cast by the Group's independent shareholders (being the shareholders excluding Virgin) in order to be valid. The outcome of both of these vote counts will be announced following the 2016 AGM.

Directors' and Officers' Liability insurance

Information on the Group's insurance cover and indemnity arrangements for liabilities that may arise against them personally in connection with the performance of their role is provided on page 136 of the Directors' Report.

Diversity policy

The Board is committed to improving diversity in its membership in the broadest sense. While any new appointments continue to be based on merit, careful consideration is given to the business benefits of improving and complementing the diversity, skills, experience and knowledge of the Board. Recruitment of an additional Non-Executive Director is underway and improved diversity will remain a key consideration.

Information on the Group's approach to diversity and inclusion and diversity initiatives, including a table detailing the number and percentage of women employed at various levels of the Group, is set out in the Strategic Report on pages 33 to 34.

Conflicts of interest

All Directors of the Group have a statutory duty to avoid any situation which might give rise to a conflict between their personal interests and those of Virgin Money. Prior to appointment, potential conflicts of interest are disclosed and assessed to ensure that there are no matters which would prevent the incoming Director from taking the appointment.

Directors are responsible for notifying the Chairman and the Company Secretary as soon as they become aware of any actual or potential conflict situations.

In addition, conflicts are monitored as follows:

- the Directors are required to declare any conflicts on appointment;
- changes to the commitments of all Directors are reported to the Board; and
- a register of potential conflicts is regularly reviewed by the Chairman to ensure the authorisation remains appropriate.

If any potential conflict arises, the relevant Director will excuse him/herself from any meeting or discussions where the potential conflicts are considered and all relevant material will be restricted, including Board papers and minutes.

All potential conflicts authorised by the Board are recorded in a register of Directors' Conflicts of Interests. This sets out the duration of the conflict, any circumstances in which the Director must revert to the Board and any conditions relating to the authorisation.

There were no potential conflicts arising in 2015 which required a relevant Director to excuse him/herself from any meeting or discussion on such matter.

Time commitments

Each Non-Executive Director is required to devote such time as is necessary for the effective discharge of their duties to a minimum of 36 days per year, including attendance at Board Committees. Non-Executive Directors may be expected to relinquish other appointments to ensure that they can meet the time commitments of their role and the requirements of CRD IV and the Senior Managers and Certification Regimes.

Fees paid to Non-Executive Directors reflect the time commitment and responsibilities of the role. The current Non-Executive Directors do not receive share options or other performance-related pay. Details of the share options granted to Sir David Clementi, the former Chairman, are set out in the Directors' Remuneration Report on page 134.

The Chairman is required to commit to Virgin Money being his primary role and limit his other commitments to ensure he can spend as much time as the role requires. Glen Moreno stood down as Chairman of Pearson plc on 31 December 2015 thereby enabling enhanced focus on Virgin Money business in 2016.

Corporate Governance Report

Executive Directors must seek authorisation from the Board before accepting any additional responsibilities or external appointments and are restricted to holding no more than two Non-Executive Director roles excluding roles with bodies not for commercial purposes. At 31 December 2015, the Executive Director was compliant with this requirement and continues to be at the date of this report.

Training

Board induction

All Directors are expected to make an informed contribution based on an understanding of the Group's business model and the key challenges it faces. The Chairman ensures that all Directors receive a full, formal and tailored induction on joining the Board, facilitated by the Company Secretary and comprising:

- a corporate induction, including an introduction to the Board and a detailed overview of the Group, its strategy, the competitive environment, operational and governance structures and main business activities;
- training on the roles and responsibilities of a Director, including statutory duties and responsibilities as an FCA approved person; and
- a detailed induction programme across Risk and Finance focusing on: risk appetite and the Group's risk profile, culture and framework, compliance and conduct risk, financial analysis and controls, capital, stress testing, liquidity, recovery and resolution planning, regulatory developments including regulatory landscape changes, governance and cultural expectations post crisis and Banking Reform Act initiatives.

The bespoke induction agreed with the Chairman is tailored to the individual needs of the Director with regard to his/her specific role and skills and experience to date. This takes the form of reading materials, meetings with members of the Board, Executive sessions with the Group's business divisions and site visits.

An enhanced induction process was undertaken for Glen Moreno in preparation for his appointment as Chairman. This included in-depth sessions with business divisions and visits to each of the Group's key sites.

On being appointed Chair of the Remuneration Committee, Marilyn Spearing attended numerous meetings with the relevant business executives including the HR Director.

Professional development

The Board receives regular training and information sessions throughout the year to address current business or emerging issues. This training is undertaken under the leadership of the Chairman and delivered through presentations and written updates by both professional advisers and members of the Executive. During 2015, training and information sessions covered a number of areas including:

- Senior Managers and Certification Regimes;
- Recovery and Resolution Planning;
- Liquidity and the liquidity regulatory agenda; and
- Capital (including stress testing requirements).

In addition, the Audit Committee hosted a series of updates on the latest accounting standards and the Board Risk Committee hosted in-depth training and guidance on cyber crime and IT security.

Directors are also invited to attend courses, management meetings and one-to-one meetings with key Executives.

Board agenda and attendance

Setting the Board agenda

The Chairman is responsible for setting the Board agenda and is assisted with this by the Chief Executive and Company Secretary. Board agendas are structured to allow adequate time for discussion of agenda items, particularly strategic matters.

Prior to each Board meeting, the Chairman reviews the agenda and time allocation with the Company Secretary and discusses key items of business with the Chief Executive. The Chairman engages with the Independent Non-Executive Directors and the Chief Executive before each scheduled meeting to discuss any matters they wish to raise.

Effective use of the Board's time

To ensure there is sufficient time allocated to formal Board business, informal additional Board time is often arranged prior to each scheduled Board meeting. This allows the Directors greater time for debate ahead of the meeting. These pre-meetings are normally attended by all members of the Board and certain members of the Executive. Occasionally, Non-Executive Director sessions, without the Executive Director, are built into the Board and Committee timetable. A key recommendation arising from the Board Effectiveness Evaluation is to optimise the Board's contribution by effective use of its time. This has been done through re-designing the forward agenda for 2016. This will balance strategic, operational and governance items, and prioritise critical issues. In addition a variety of Board forums, including Chief Executive/Chairman/Independent Non-Executive Director only meetings and Non-Executive Director only meetings have been scheduled throughout 2016.

Attendance at meetings

The attendance of Directors at Board and Committee meetings during the year is set out below. The number of meetings held during the period that the Director held office is shown in brackets. While Directors may be invited to, and regularly attend other Board Committee meetings, only attendance at Board Committees of which Directors are members is recorded in the below table.

In 2015, a total of thirteen Board meetings were held, ten of which were scheduled and three were ad hoc meetings. Ad hoc Board meetings are called on short notice to discuss a matter that cannot wait until the next scheduled meeting. Where a Director is unable to attend a meeting, the Chairman discusses the matter with the Director and seeks his/her views for the proposed resolutions. He also represents his/her views at the meeting. Also, any Director unable to attend a meeting has the opportunity to review any papers and provide comments to the Chairman.

Virgin Money Holdings (UK) plc	Scheduled Board meetings	Additional Board meetings	Remuneration Committee	Nomination Committee	Board Risk Committee	Audit Committee	Balance Sheet Committee[1]
Current Directors who served during 2015							
Glen Moreno	10 (10)	3 (3)	–	4 (4)	–	–	–
Norman McLuskie	10 (10)	3 (3)	7 (7)	6 (6)	5 (5)	9 (10)[2]	1 (2)[2]
Colin Keogh	10 (10)	3 (3)	–	6 (6)	5 (5)	10 (10)	2 (2)
Marilyn Spearing	10 (10)	3 (3)	7 (7)	3 (3)	5 (5)	10 (10)	2 (2)
Geeta Gopalan (appointed 25 June 2015)	4 (4)	2 (2)	2 (2)	1 (1)	1 (2)[3]	3 (4)[3]	–
Gordon McCallum	10 (10)	2 (3)[4]	–	5 (6)[4]	–	–	–
Patrick McCall	10 (10)	1 (3)[5]	–	–	–	–	–
Jayne-Anne Gadhia CBE	10 (10)	3 (3)	–	–	–		–
Former Directors who served during 2015							
Sir David Clementi (retired 30 June 2015)	6 (6)	1 (1)	4 (4)	2 (3)[6]	–		–
James B Lockhart III (retired 11 September 2015)	7 (7)	2 (2)	–	4 (4)	–		–
Lee Rochford (retired 31 August 2015)	7 (7)	1 (1)	–	–	–		–
Olivia Dickson (retired 31 December 2015)	10 (10)	3 (3)	7 (7)	6 (6)	4 (5)[7]	–	2 (2)

1 The Balance Sheet Committee and Board Risk Committee were consolidated into a single Board Risk Committee in June 2015.

2 Apologies due to illness.

3 Conflict with external appointments.

4 Conflict with an external appointment.

5 Conflict with external appointments and meetings arranged at short notice.

6 Conflict with an external appointment.

7 Conflict with an external appointment.

Corporate Governance Report

Effectiveness

Board effectiveness

Background

The Board engaged an external facilitator, Dr Tracy Long CBE of Boardroom Review Limited, for the Group's Board and Committees effectiveness review. Boardroom Review, which has no other connection with the Group, has extensive experience working with publicly listed organisations and Dr Long is considered to be a leader in the field of board evaluation.

The process was co-ordinated by the Chairman and Company Secretary who together provided a comprehensive briefing to Dr Long. A summary of the evaluation methodology, process followed, conclusions and the Board roadmap (priorities and recommendations) are set out below.

Evaluation methodology and process

The methodology for the review was designed to provide an exchange of ideas and opinions between the reviewer and the Directors and a constructive and ongoing dialogue between Board members.

- **Themes** – The review examined use of Board time, quality of information received, Board contribution (including culture and dynamics), composition and Board areas and depth of engagement (strategy, risk and control and people).
- **Evidence** – Copies of Board and Committee papers and key governance materials were reviewed. Detailed interviews were conducted with each Board member, the CFO, Chief Risk Officer, HR Director, Chief Banking Officer and Company Secretary. The September 2015 Board and Committees were observed to witness first-hand boardroom dynamics and effectiveness.
- **Independent view** – An analysis of strengths and challenges, priorities and objectives was undertaken.
- **Prioritisation and roadmap** – A draft discussion document, containing analysis, personal opinion and recommendations based on best practice as detailed in the Code and other current guidelines, was discussed with the Chairman. This was followed by individual meetings with all participants, during which feedback on individual performance and suggestions for improvement was provided. The outcome of the evaluation was discussed with the Board in November 2015, at which Dr Long presented her findings and the Board agreed the roadmap for its development.

Key conclusions

- A well balanced Board in terms of skills, experience and independence;
- An engaged, experienced and inclusive Chairman with strong sector knowledge and a supportive and consultative relationship with the Chief Executive was also recognised;
- Chairman is focusing on refining the Board's role and use of its time to drive increased Board engagement and added value;
- The Chief Executive is commended for her integrity and leadership and as a good ambassador and strong customer advocate;
- Transparent information flow and open access between Non-Executive Directors and the Executives;
- Board processes are becoming more efficient with high quality information and excellent secretarial support, contributing to the efficiency of meetings;
- An open culture, diversity of opinion and committed contribution by all members;
- Appropriate focus on strategy, risk and control and remuneration with a shared view of the strategic challenges faced by the business;
- The risk and control framework was considered a particular strength with a strong and distinctive corporate culture with declared values, principles and behaviours evident; and
- A straightforward and disciplined approach to remuneration, aligned with shareholder interests.

Follow up

The results of the evaluation process formed part of the Chairman's appraisal of the overall effectiveness of the Board, its members and the annual effectiveness review of each of the Board Committees. The Chairman has discussed with individual Directors any specific training or development needs arising from the review. Dr Long will meet again with the Chairman in six to twelve months' time to discuss progress made against the roadmap.

Roadmap – priorities and recommendations/actions taken in response

A need to balance strategic, operational and governance items and prioritise critical issues.

- The 2016 forward agendas have been developed through a collaborative process, and consultation between the Chairman, Non-Executive Directors, Chief Executive and Company Secretary.
- A variety of Board forums, including Chief Executive/Chairman/Non-Executive Director meetings and Non-Executive Director-only meetings have been built into the 2016 Board schedule facilitating engagement outside of the formal Board/Committee forums.

The importance of the Board as a team.

- The Board has to function well as a team, with a healthy balance of challenge and support. The approved statement of responsibilities for Senior Managers and revised role profiles for all Non-Executive Directors set clear expectations.
- The Chairman will continue to focus on creating a strong Board culture with mutual trust and respect, open communications, challenge and support.

Greater clarity and visibility on Board succession and appointment.

- The Board is enhancing the medium-term succession plan to provide clear succession for Non-Executive Directors, Committee Chairs and key members of the Executive. A skills matrix and refresh plan is under development to align with current and future strategy recognising the need for diversity, experience, desired behaviours and culture.
- The Chairman has formalised the key internal appraisal processes and appointment processes agreed with the Nomination Committee for recruitment and tenure planning.

Deeper focus on the external landscape (market environment, competition, regulatory agenda).

- There is a shared recognition between the Non-Executive Directors that greater time is needed on the external environment. In addition to its current assessment of the evolving external environments and the Group's competitive position, a series of deep dive briefings on the external market and regulatory environment with a focus on threats and opportunities are to be scheduled.

Need for increased time on scenario planning or crisis management.

- As the Group grows its business, the risk agenda will develop with increased focus on scenario planning and crisis management and identification of risk priorities.

Continued focus on leadership and ensuring that talent development and succession planning are aligned with the current and future strategy.

- The Chairman and Chief Executive will continue to identify certain individuals (internally or externally) with the potential to take on the Chief Executive role in the future and ensure the Nomination Committee is prepared for Chief Executive succession.
- The Board will continue to review the senior talent and diversity, succession and development plans on an annual basis. The reviews will include analysis of the key (internal and external) competencies required, available options and individual development plans.

Shareholder engagement and relationships

The Board recognises the need for a programme of engagement which offers all shareholders opportunities to receive information directly and enable them to share their views with the Board.

The Chairman and Chief Executive have an ongoing dialogue with the Virgin nominee director in respect of the Board agenda.

During the year FMR LLC, Kames Capital plc and BlackRock, Inc have increased their shareholdings in the Company to 7.71%, 3.25% and 5.01% respectively.

Please see page 287 for details of the break down of the Company's share register.

Controlling shareholders

During 2015 the Group's "controlling shareholders" were Virgin and WLR. The Group is party to relationship agreements with each of Virgin and WLR (Relationship Agreements). The principal purpose of the Relationship Agreements is to ensure that Virgin Money is capable of carrying on its business independently of its controlling shareholders. The Relationship Agreements provide for the appointment of a nominee director by each of Virgin and WLR through whom the Chairman and other Non-Executive Directors are kept up to date during the year with the views of such shareholders.

Corporate Governance Report

WLR ceased to be a "controlling shareholder" (for the purposes of the Listing Rules) on 20 April 2015 when WLR sold 45 million ordinary shares, reducing its shareholding to 23.3 per cent. In September, WLR sold down a further tranche of shares resulting in a reduction of its shareholding to 12.0 per cent and at the same time WLR's nominee director, James B Lockhart III, also stepped down as a Non-Executive Director. As a consequence of WLR ceasing to be a "controlling shareholder", a number of the terms of the Relationship Agreement between the Group and WLR ceased to apply save for certain information rights and the right to appoint a nominee director which WLR has currently chosen not to exercise.

Under the Relationship Agreement with Virgin, Virgin has undertaken that it shall not:

- take any action that would preclude or inhibit any member of the Group from operating independently of Virgin;
- take any action that would prevent Virgin Money from complying with its obligations under the Listing Rules;
- propose any shareholder resolution which is intended to circumvent the Listing Rules;
- conduct any transactions and arrangements with the Group other than on an arms' length basis and on normal commercial terms;
- exercise any voting or other rights and powers to procure or propose, or vote in favour of, any resolution for an amendment to the Articles which would breach the provisions of the Relationship Agreement or the Listing Rules or the Disclosure and Transparency Rules (DTR), or would prevent the Group from carrying on business independently of Virgin;
- act in any way which it knows will render Virgin Money unsuitable for continued listing on the London Stock Exchange; and
- vote on any resolution to approve a "related party transaction" where Virgin is the related party.

So far as the Company is aware, the independence provisions outlined above have been complied with by Virgin and by WLR whilst in place, and the Company has complied with the terms of the Relationship Agreements.

Investor relations

The Investor Relations Director has primary responsibility for day-to-day communications with existing shareholders, potential investors and analysts. Supported by the Chief Executive and CFO as well as other executives as required, these communications are effected through a combination of briefings to analysts and institutional investors, individual discussions with shareholders and potential investors, regulatory announcements, press releases and updates on the Virgin Money website.

The Investor Relations Director reports regularly, and on an ad hoc basis as appropriate, to the Board to ensure it is informed of significant market developments, share price performance and changes in the shareholder base. In addition, the Board receives regular updates from the Group's corporate brokers.

Investor contact

In 2015, the Group has engaged in active discussions with shareholders and potential investors, both on an individual basis and through attendance at investor conferences. The Group intends to develop its investor communications programme further in 2016. The Group will maintain an active dialogue with shareholders, potential investors and analysts to discuss the performance of the Group, its strategy and new developments.

Additionally, the Group engaged with institutional investors or their representatives on governance and remuneration matters in advance of the 2015 AGM and will continue to do so in future.

The Group has an Investor Relations section on its website which contains information on all disclosures made to the market, including results presentations, annual reports, interim results and trading statements.

Shareholders, potential investors and analysts are able to ask a question on the Group through the Investor Relations function or the Group Secretariat.

The Senior Independent Director is available to shareholders which contact through the normal channels of Group Chairman, Chief Executive, CFO or other executives cannot resolve, or for which such contact would be inappropriate. He may be contacted through the Company Secretary at Jubilee House, Gosforth, Newcastle upon Tyne, NE3 4PL.

Company Secretary and retail shareholders

The Company Secretary oversees communication with individual retail investors (the vast majority of whom are currently colleagues although there has been a broadening of the shareholder base throughout 2015).

The Group's registrar, Equiniti Limited, provides a dedicated shareholder online dealing service to assist shareholders in managing their investments. Investors can also manage their shareholdings over the telephone.

During the year the Group has made specific contact with shareholders in relation to, amongst others, a bank mandate collection exercise for the purpose of payment of the 2015 interim dividend and payment of the interim dividend itself.

The Annual General Meeting

The AGM is the principal opportunity for shareholders to engage directly with the Board. It is more commonly used by retail shareholders as an opportunity to share views and raise questions during the meeting, but afterwards there is the opportunity to meet the Directors and members of the Executive.

The Company's first AGM was held in London in May 2015 and in excess of 80% of total voting rights were voted by shareholders.

All Board members attended the 2015 AGM and plan to attend the AGM in 2016. All shareholders will be invited to attend the AGM in 2016. The 2016 AGM will be held on 4 May 2016 at the London offices of Allen & Overy LLP. Information on the business to be considered at the AGM will be set out in the Notice of Meeting which will be issued to shareholders, together with any related documentation, in due course.

Internal control

The Board is responsible for the Group's system of internal control. The system is designed to facilitate effective and efficient operations and to ensure the quality of internal and external reporting and compliance with applicable laws and regulations. The Directors and senior management are committed to maintaining a robust control framework as the foundation for the delivery of effective risk management. The Directors acknowledge their responsibilities in relation to the Group's systems of risk management and internal control and for reviewing their effectiveness and conducted such a review during the year.

In establishing and reviewing the system of internal control, the Directors consider the nature and extent of the risks facing the Group, the likelihood of a risk event occurring and financial impact of failure. A system of internal control is designed to manage, rather than eliminate, the risk of failure to achieve business objectives. It can therefore provide only reasonable but not absolute assurance against the risk of material misstatement or loss.

The policies supporting the Group's risk management framework define minimum standards for controls for all material risk classes.

Business areas and support functions assess quarterly the internal controls in place to address all material risk exposures across all risk classes. This review considers the effectiveness of these material controls, including financial, operational and compliance controls.

An independent external assessment of the effectiveness of the Internal Audit function was carried out by Deloitte LLP (Deloitte) in the fourth quarter of 2015. Details of the key findings are set out in the Audit Committee Report on page 101.

Further information on the risk control and management is set out in the Risk Management Report on pages 139 to 208.

Statement of compliance

UK Corporate Governance Code

The 2014 Code applied to the Group's 2015 financial year. The Directors have considered the contents and recommendations of the Code and confirm that throughout the year Virgin Money has applied the main principles and complied with the provisions of the Code.

The British Bankers' Association Code for Financial Reporting Disclosure

Virgin Money has adopted the British Bankers' Association Code for Financial Reporting Disclosure and its 2015 Annual Report has been prepared in compliance with its principles.

Committee reports

The following pages contain reports from each of the Board's Committees.

Corporate Governance Report

Nomination Committee Report

"In 2015 we continued to work hard on the composition of the Board to optimise its effectiveness and support our corporate strategy."

Glen Moreno
Chair, Nomination Committee

Membership and meetings

	Independent	Meetings attended/ held in 2015[1]
Committee Chair		
Glen Moreno (appointed 21 May 2015)	Yes	4 (4)
Committee members		
Colin Keogh	Yes	6 (6)
Norman McLuskie	Yes	6 (6)
Gordon McCallum	No	5 (6)[2]
Marilyn Spearing	Yes	3 (3)
Geeta Gopalan (appointed 25 November 2015)	Yes	1(1)
Former Committee members		
Sir David Clementi (retired 30 June 2015)	No	2 (3)[3]
James B Lockhart III (retired 11 September 2015)	No	4 (4)
Olivia Dickson (retired 31 December 2015)	Yes	6 (6)

1 Number of meetings held during the period the member held office.
2 Conflict with an external appointment.
3 Conflict with an external appointment.

Chairman's overview

During 2015, the Nomination Committee continued to keep under review the Group's governance arrangements, including Board composition, succession planning and the effectiveness of the Board and Bank Board and their Committees.

The Committee recommended that the Board appoint Geeta Gopalan as a new Independent Non-Executive Director. The Committee also recommended the appointment of Peter Bole as CFO, following Lee Rochford's decision to leave the business in August 2015. It is expected that Peter will join the business in 2017, following which he will be appointed as an Executive Director. More on the appointment of Geeta and Peter can be found in this report.

In November the Committee recommended the appointment of Marilyn Spearing (a Director since January 2014) as Chair of the Remuneration Committee, following the retirement of Olivia Dickson from the Board on 31 December 2015.

The Committee also noted the retirement in May of Sir David Clementi as Chairman and the retirement of James B Lockhart III, WLR's nominee director, from the Board and Committee in September 2015, following the reduction in WLR's shareholding from 33.5% to 12%. The Committee continually considers Board composition, tenure and succession plans and aims to appoint an additional Independent Non-Executive Director in 2016.

During the year, the Committee commissioned an externally-facilitated evaluation of the Board and Committees' effectiveness. The review, carried out by Boardroom Review Limited, offered an independent view of the Board's effectiveness and has provided the Board with a roadmap for Board and Committee development. Details of the review can be found on pages 92 to 93.

The Committee considered management's succession planning and oversaw the strengthening of the Executive. Details can be found on pages 97 to 98. Together, the Directors and Executive continue to bring a wealth of experience and expertise to the management and operations of the Group.

The Committee monitored changes in regulations, most notably the requirements arising from the new Senior Managers and Certification Regimes to be implemented in March 2016. This included the approval of the new statements of responsibilities and associated role profiles for each of the Non-Executive Directors who will be Senior Managers.

Nomination Committee Report

Committee purpose and responsibilities

The purpose of the Committee is to keep the Board's composition, skills, experience, knowledge, independence and succession arrangements under review. The Committee makes recommendations to the Board to ensure that the Group's arrangements are consistent with good corporate governance standards. The Committee's role also extends to appointments to the Board of the Group's material subsidiaries including the Bank.

Examples of how the Committee discharged its responsibilities during the year are set out below. Full details of the Committee's responsibilities are set out in the Committee terms of reference (which were updated in January 2016) and can be found on the website at virginmoney.com/virgin/investor-relations.

During the year the Committee met its key objectives and carried out its responsibilities effectively, as confirmed by the annual effectiveness review.

Committee composition, skills and experience

To ensure a broad representation of independent views, including perspectives from each of the Committees, membership of the Nomination Committee comprises the Chairman, all Independent Non-Executive Directors (Geeta Gopalan joined the Committee in November 2015) and the Virgin nominee director. Geeta's perspective and experience gained from being a Non-Executive Director on other boards as well as her prior executive career further complements the composition of the Committee. The Chief Executive and, if required, the HR Director attend meetings as appropriate.

How the Nomination Committee spent its time in 2015

Board and Executive succession

The Committee:

- oversaw the Board's arrangements for the longer-term succession of Board and Committee members. Non-Executive Director succession planning is addressed as part of the ongoing review of Board composition. The approach takes into account the need to refresh the intake of Non-Executive Directors to bring new and diverse perspectives to the Board and its decision making. It also ensures appropriate representation on each of the Board's Committees and planning for longer term succession. Work is underway to assess the collective technical and governance skills required from the Non-Executive Directors to support the future business strategy, with the aim to develop a skills matrix to enable enhanced longer-term succession planning;
- considered the adequacy of succession arrangements for the Executive Director and members of the Executive. The Chairman is responsible for developing and maintaining a succession plan in relation to the Chief Executive, who is in turn primarily responsible for developing and maintaining a succession plan for key leadership positions in the Executive team. Following a review of the structure and succession planning of the Executive, Hugh Chater has been appointed as Chief Commercial Officer with responsibilities for the full range of existing Virgin Money products, including credit cards. He will join the business by June 2016 and brings deep experience of retail banking;
- began a process of strengthening the composition, diversity and experience of the Board leading to the appointment of Geeta Gopalan as a Non-Executive Director on 25 June 2015. Egon Zehnder, an external search consultant with no other connection to the Group, was appointed to assist in the identification of appropriate candidates. Details of Geeta's experience are set out on page 76;
- recommended the appointment of Marilyn Spearing as Chair of the Remuneration Committee in place of Olivia Dickson. Marilyn has been a member of the Remuneration Committee since January 2014 and brings a wealth of experience in managing organisational, operational and structural change and has a deep understanding of remuneration and risk governance; and
- in January 2016 recommended the appointment of Peter Bole as CFO. Details of the recruitment process are set out on page 98.

The Committee and the Board are satisfied that the Executive is staffed appropriately and the Committee will continue to ensure robust succession planning remains under review.

Corporate Governance Report

Nomination Committee Report

Recruitment of Chief Financial Officer

During the second half of 2015 the search for a CFO was commenced. Odgers Berndtson (Odgers) was appointed to support the executive search on the basis of their strength in finance appointments and their overall market reputation. Odgers has no other connection with the Group.

A specification for the role and profile of the candidate was agreed by the Committee in conjunction with the Chief Executive. Key attributes for the position include a focus on financial technical strength, credibility as an Executive Director of the Group, executive leadership capability and market impact.

Odgers analysed the market for possible candidates with a breadth of diversity, experience and background. A short list was produced from which four potential candidates were interviewed by a combination of the Chief Executive, Chairman, SID and HR Director. Following this comprehensive search process overseen by the Committee, Peter Bole was appointed CFO. Peter is expected to join Virgin Money as CFO in 2017, following which he will be appointed as an Executive Director.

Peter brings with him extensive experience in UK retail banking. He is currently CFO of Tesco Bank, where he has led the Finance Function since 2009. Peter has previously held various senior roles in the finance function at RBS, where he was involved in the migration of Tesco Personal Finance. Dave Dyer, who was appointed CFO in August 2015, following Lee Rochford's decision to leave the business, will continue to hold the position until he hands over responsibilities to Peter ensuring continuity whilst succession is enabled.

Composition, skills and independence

The Committee is responsible for the ongoing assessment of the independence of the Non-Executive Directors, the re-appointment or re-election of Directors and their suitability to continue in office.

In assessing independence, the Committee considered both the Code requirements on independence and factors such as length of tenure and ability of the Non-Executive Directors to provide an objective challenge to the Executive, free of relationships and other circumstances that could affect their judgement. It also took account of any relationships that had been disclosed and authorised by the Board. Based on its assessment for 2015, the Committee is satisfied that, throughout the year (or their period of appointment), Colin Keogh, Norman McLuskie, Marilyn Spearing and Geeta Gopalan remained independent as to both character and judgement and that Glen Moreno was considered independent on his appointment. The nominee director (Gordon McCallum) is not considered to be independent due to his relationship with the Group's controlling shareholder, Virgin. Patrick McCall is not considered to be independent since he was appointed to the Board as the representative director of Virgin Enterprises Limited (VEL) pursuant to the Virgin Money Trade Mark Licence Agreement.

The Committee reviewed the role, including capabilities and time commitments of the Chairman, SID, Non-Executive Directors and the Chief Executive. In particular, the Committee considered the impact of limits placed by CRD IV on the number of directorships that can be held by the Directors.

The Committee is comfortable to recommend the re-election or election of all Directors, as at the date of this report, to shareholders at the forthcoming 2016 AGM.

Effectiveness

Details of the methodology, process followed, conclusions and key recommendations from the Board Effectiveness Evaluation is set out in the case study on pages 92 to 93 of the Corporate Governance Report.

The key conclusion of the review, which formed the basis of the Board and Committee annual effectiveness review, was that the Board and Committees continue to operate effectively, although there are opportunities to improve effectiveness.

The Committee will monitor the Board's progress against the agreed roadmap (recommendations and priorities) in 2016, with the Chairman scheduled to meet again with Dr Long in six to twelve months' time to discuss progress made and actions taken against the recommendations.

Nomination Committee Report

Diversity

During the course of the year, the Board reviewed the Group's performance against the Board approved Diversity Policy. The policy sets out the approach to diversity for each of the main Boards within the Group. Under the Board Diversity Policy, the Committee is responsible for reviewing the composition of the Group's Boards to ensure that membership reflects diversity in the broadest sense. The combination of personalities on the Boards provides a good range of perspectives and improves the quality of decision making.

In 2015, the Board continued to focus on improving diversity. The percentage of female representation on the Board significantly exceeds the objective of 25% set out in the Board Diversity Policy and exceeds the Davies Report requirements. The revised Board Diversity Policy will introduce a long-term objective of gender equality and a focus on other forms of diversity on the Board.

Achieving full compliance with the Board Diversity Policy is a continual focus and one which the Committee will monitor during 2016, as the search for an additional Non-Executive Director gets underway.

Please see pages 33 to 34 of the Strategic Report for details of the Group's Diversity Policy as a whole.

Glen Moreno
Chair, Nomination Committee

1 March 2016

Corporate Governance Report

Audit Committee Report

"In 2015, the Audit Committee has overseen the Group's first full annual cycle of financial reporting as a listed company and a robust external audit tender process."

Norman McLuskie
Chair, Audit Committee

Membership and meetings

	Independent	Meetings attended/ held in 2015[1]
Committee Chair		
Norman McLuskie	Yes	9 (10)[2]
Committee members		
Colin Keogh	Yes	10 (10)
Marilyn Spearing	Yes	10 (10)
Geeta Gopalan (appointed 25 June 2015)	Yes	3 (4)[3]

1 Number of meetings held during the period the member held office.

2 Apologies due to illness.

3 Conflict with an external appointment.

Chairman's overview

The Audit Committee has fulfilled its responsibilities and met its key objectives, as confirmed by the annual effectiveness review.

A formal competitive tender for external audit services was undertaken during the year. The Committee oversaw the tender process which involved a thorough and robust assessment of the firms involved, including the incumbent firm (KPMG), details of which are set out on page 102.

After careful consideration of the strength of each proposal, the Board accepted the recommendation from the Committee to appoint PwC as external auditor for the year ending 31 December 2016. Accordingly, subject to shareholders' approval, PwC will be appointed as auditor for the 2016 financial year.

The Committee would like to thank KPMG for their significant contribution as auditor and for their consistently high standards of professionalism in executing the role.

The Committee reviewed a number of key accounting judgements relevant to the financial statements, including a focus on the calculation of effective interest rate, impairment provisioning, cost capitalisation, deferred tax and fair values of financial instruments. A key addition to the 2015 Annual Report is the inclusion of a viability statement as required by the Code. This can be found within the Risk Overview section on pages 52 to 53.

The Committee oversaw the process for the recruitment of the new Internal Audit Director, David Barnes, who was appointed to the role in May 2015. The Committee continues to be satisfied with the activity, role and effectiveness of the internal audit function. This view was reinforced by the conclusions from the independent review carried out by Deloitte LLP in the final quarter of 2015, details of which are set out on page 101.

Committee purpose and responsibilities

The purpose of the Committee is to monitor and review the Group's financial reporting arrangements, the effectiveness of its internal controls and risk management framework, the internal and external audit processes and the Group's whistleblowing procedures. The Committee reports to the Board on its activities and makes recommendations, all of which have been accepted during the year.

The key activities of the Committee are set out below and a full list of the Committee's responsibilities is detailed in the Committee's terms of reference (which were updated in January 2016) and can be found on the website at virginmoney.com/virgin/investor-relations.

Committee composition, skills and experience

The Committee acts independently of management. This ensures that the interests of shareholders are properly protected in relation to financial reporting and internal control. Following the appointment of Geeta Gopalan as a member, the Committee now comprises four Independent Non-Executive Directors with recent and relevant experience in finance and/or banking. Norman McLuskie is a chartered accountant and has significant financial and banking experience in the UK listed environment enabling him to fulfil the role as Audit Committee Chair. The Chairman, Chief Executive, CFO, Chief Risk Officer and Internal Audit Director attend committee meetings. The external auditor also attends.

Audit Committee Report

How the Committee spent its time in 2015

Financial reporting

A key responsibility of the Committee is to review the content of the Annual Report, interim accounts and quarterly trading statements. In doing so, the Committee:

- reviewed the Annual Report to ensure that, taken as a whole, based on the information supplied to it and challenged by the Committee and on its judgement is fair, balanced and understandable and advised the Board to that effect;
- reviewed and challenged the going concern and viability assessment undertaken by management. Further detail can be found on pages 52 to 53;
- reviewed and challenged, where necessary, the actions, estimates and judgements of management; and
- monitored the integrity of the financial statements of the Group and reviewed the critical accounting policies, disclosure obligations and changes in accounting requirements.

The Committee also ensured that the Group's Pillar 3 disclosures satisfied the prescribed requirements.

Internal control and risk management

Full details of the internal control and risk management systems in relation to the financial reporting process are given within the Corporate Governance Report at page 95 and the Risk Management Report on pages 145 to 149. Specific matters that the Committee considered during the year included:

- the effectiveness of systems for internal control, financial reporting and risk management;
- the extent of the work undertaken by the finance teams and considering the resources required to be deployed to ensure that the control environment continued to operate effectively; and
- the major findings of internal investigations into control weaknesses, fraud or misconduct and management's response alongside any control deficiencies identified.

The Committee is satisfied that internal controls over financial reporting and risk management systems were appropriately designed and operating effectively during the period under review.

Internal audit

In monitoring the activity, role and effectiveness of the internal audit function and their audit programme, the Committee:

- considered the effectiveness of the function, including the commissioning of an independent external assessment, carried out by Deloitte LLP, which concluded that the function generally conforms with the Standards and Code of Ethics issued by the Chartered Institute of Internal Auditors (CIIA). Some areas were identified where further work is needed to conform fully to some of the more challenging areas of the CIIA's 2013 Guidance, "Effective internal audit in the financial services sector". A prioritised action plan has been prepared to address these areas;
- approved the audit plan and budget and monitored progress against it at regular intervals, confirming that appropriate resources and capability were in place to execute the plan effectively and considered internal audit to have sufficient standing in the Group;
- considered the regular internal audit reports, including thematic and routine reviews on prudential and regulatory compliance, customer conduct, credit risk, IT and financial controls, discussing major findings and management's responses; and
- oversaw the process for recruitment of a new Internal Audit Director, and approved the appointment of David Barnes to the role.

Whistleblowing

The Committee received and considered reports from internal audit on the Group's whistleblowing arrangements including line activity and ongoing reviews of the revised whistleblowing policy and governance structure.

The Committee considered the PRA and FCA policy statements containing new rules on whistleblowing published in October 2015. The Chair of the Committee has been appointed as the whistleblowing champion and a review of the Group's processes is underway to ensure compliance with the new regime by September 2016.

Corporate Governance Report

Audit Committee Report

External audit

The Committee oversaw the relationship with the external auditor and considered the terms of engagement (including remuneration), their effectiveness, their continued independence and their objectivity. In particular, the Committee:

- approved the annual audit plan and negotiated and agreed the auditor's remuneration;
- reviewed the findings of the external audit including key judgements and the level of challenge produced by the external auditor;
- considered management's responsiveness to the external auditor's findings and recommendations; and
- considered the continued effectiveness of the audit process and the external auditor's performance, including technical competence, strategic knowledge, quality control, communication and reporting through an internal effectiveness review.

Auditor tenure

The Committee took the decision in the first quarter of 2015 to tender the audit of the Group. The tender resulted in the Board accepting the recommendation from the Audit Committee to appoint PwC as external auditor for the year ending 31 December 2016, subject to shareholders' approval at the 2016 AGM. Further detail of the process is given in the case study below.

The Committee is satisfied that the Company has complied, during the financial year under review and up to the date of this report, with the provisions of the Statutory Audit Services for Large Companies Market Investigation (Mandatory Use of Competitor Tender Processes and Audit Committee Responsibilities) Order 2014.

External Audit Tender

Background

Virgin Money appointed KPMG as its external auditor in 2004. KPMG was approved as auditor of the enlarged Virgin Money Group in 2012, following the acquisition of Northern Rock plc. Although a review of the audit arrangements took place at the time, no formal audit tender was undertaken. The Committee confirmed in the Group's 2014 Annual Report that, in light of developments in relation to the reform of the external audit market, the Committee would undertake a formal competitive tender in 2015, with a view to appointing a new audit firm, or re-appointing KPMG, for the 2016 external audit.

In June 2015, the Committee took the decision to invite KPMG, PwC, Deloitte and Ernst & Young LLP to tender for the Group audit on the grounds that they each have the technical expertise, resources and national coverage required to provide a comprehensive service to the Group.

Governance

The proposal to tender was overseen by the Committee. Audit tender processes are time consuming; as a result, the Committee was mindful to use a concise yet thorough process. The tender process involved five key stages, which are summarised below:

Stage 1 – initial management meeting.
The non-incumbent firms each met with the Chief Executive, Chair of the Audit Committee, CFO and Finance Director (the "Selection Panel"). These sessions allowed the Group to gain insight into the experience, qualification and fit of the proposed audit teams;

Stage 2 – request for proposal (RFP).
An RFP was issued to KPMG and two other firms which included guidance on the selection criteria and a request to provide detailed information on matters which were key to the Committee's assessment of each bid. This included: confirmation of the proposed audit team, an outline of the proposed audit and transition approach, a summary of the proposed fees, evidence of the firm's cultural alignment to Virgin Money and details of any value added services or additional features that would be provided as part of the service;

Stage 3 – stakeholder engagement for non-incumbent firms.
To increase business understanding and build relationships, the remaining two non-incumbent firms met with a number of the Group senior management team. KPMG had access to the same stakeholders as part of their ongoing audit role;

Stage 4 – submission of a written proposal document.
The participant firms submitted their written proposal documents and supporting due diligence information to the Group. These documents were assessed and rated against the selection criteria which involved qualification, expertise, resources and cost; and

Stage 5 – tender presentations.
The participant firms presented their audit proposals to the Selection Panel which, at this stage, also included the Chair of the Board Risk Committee.

Throughout the process, the Committee was mindful of the need to preserve the independence of the external audit. As a result, at the outset, each firm was required to disclose all existing relationships with the Group and explain their proposals for ensuring that those relationships would not cause any conflict of interest after 1 January 2016, were the firm to be appointed as auditor.

Outcome

After careful consideration of each proposal, the Board accepted the recommendation from the Committee to appoint PwC as external auditor for the year ending 31 December 2016. Accordingly, subject to shareholder approval at the AGM in 2016, PwC will be appointed as external auditor for 2016.

Audit Committee Report

Auditor independence and remuneration for non-audit services

Both the Board and the external auditor have safeguards in place to protect the independence and objectivity of the external auditor. The Committee has a comprehensive policy, refreshed in 2015, to regulate the use of the auditor for non-audit services. This policy sets out the nature of work that the external auditor may not undertake, including financial information system design and implementation.

In some cases, the external auditor may be selected over another service provider due to their detailed knowledge and understanding of the business. Any allowable non-audit services with a value above £250,000 requires approval from the Audit Committee Chair. The total amount paid to the external auditor in 2015 was £1.3 million. Details of the payments for audit and non-audit service provided in 2015 is shown in note 6 to the financial statements.

An additional policy on the employment of former external auditor's staff is in place to further preserve the independence of the external auditor.

Financial reporting

During 2015, the Committee considered the following key financial issues and judgements in relation to the Group's financial statements and disclosures, with input from management and the external auditor:

Key issues/judgements in financial reporting	Audit Committee review and conclusions
Effective Interest Rate (EIR) The application of the EIR method of accounting is judgemental and requires management to make a number of assumptions.	Interest earned on loans and receivables is recognised using the EIR method. EIR is calculated on the initial recognition of mortgage and credit card lending through a discounted cash flow model that incorporates fees, costs and other premiums or discounts. There have been no changes to the EIR accounting policies applied for mortgages and credit cards during the year. The Committee spent time understanding and challenging the judgements taken and the EIR methodology applied by management including expected future customer behaviours. Time was also spent considering the appropriate EIR methodology for credit cards in light of the planned growth in balances. The Committee agreed that management's judgement was appropriate as at 31 December 2015. The disclosures relating to EIR are set out in note 1.10 to the financial statements.
Allowance for impairment losses on loans and receivables Determining the appropriateness of impairment losses is judgemental and requires the Group to make a number of assumptions.	The Committee received regular reports from management in relation to impairment provisioning for the secured and the unsecured credit portfolio. The Committee considered and challenged the provisioning methodology applied by management, including the results of statistical loan loss models to support the impairment provisions. The Committee considered the calibration of model parameters in the light of economic indicators including house price movements, and underlying book performance. The Committee was satisfied that the impairment provisions, including management's judgements, were appropriate. The disclosures relating to impairment provisions are set out in note 1.10 to the financial statements.

Corporate Governance Report

Audit Committee Report

Key issues/judgements in financial reporting	Audit Committee review and conclusions
Capitalisation and impairment of intangibles Determining the appropriateness of costs that qualify for recognition as intangible assets requires management judgement. Management are also required to make ongoing assessments of whether any assets are impaired. No assets were identified as impaired through reviews for indicators of impairment.	Over the course of 2015 there has been significant investment spend, in particular in relation to new office software for employee workstations and further development of the Group's digital banking channel. The Committee has considered and is satisfied with the appropriateness of the accounting recognition of these investment costs, including those costs that qualify for recognition as intangible assets in line with the criteria prescribed by accounting standards. The Committee has also considered management's reviews for indicators of impairment and is satisfied with the conclusion that no assets require impairment adjustment. The disclosures relating to the movement in intangible asset balances during the year are set out in note 1.10 to the financial statements.
Recoverability of the deferred tax asset The Group continues to recognise deferred tax assets and liabilities in respect of timing differences in the main trading subsidiaries. Based on the Group's forecast taxable profit, the losses are expected to be fully utilised in the near to medium term.	The Committee considered the recognition of deferred tax assets, in particular the forecast taxable profits based on the Group's three-year strategic plan. The Committee agreed with management's judgement that the deferred tax assets were appropriately supported by forecast taxable profits, taking into account the Group's long-term financial and strategic plans. This assessment incorporated impacts of the tax measures and surcharge on banking profits announced by the Chancellor of the Exchequer in the 2015 Summer Budget Statement. The disclosures relating to deferred tax assets are set out in note 1.10 to the financial statements.
Fair value of financial assets and liabilities The Group use estimates and judgements in the calculation of fair values for assets and liabilities where not all inputs to calculations are observable in the market, or where there are factors specific to an individual instrument that impact fair values.	The Committee spent time understanding and assessing judgements applied and agreed with management's judgement regarding the calculation of fair values in 2015. The disclosures relating to fair value are set out in note 1.10 to the financial statements.

Norman McLuskie
Chair, Audit Committee

1 March 2016

Board Risk Committee Report

"Our priority is ensuring that risk management is at the heart of our strategic delivery."

Colin Keogh
Chair, Board Risk Committee

Membership and meetings

	Independent	Board Risk Committee Meetings attended/ held in 2015[1]	Balance Sheet Committee Meetings attended/ held in 2015[1]
Committee Chair			
Colin Keogh (Risk Committee)	Yes	5/5	2/2
Norman McLuskie (Balance Sheet Committee)	Yes	5/5	1/2[2]
Committee members			
Marilyn Spearing	Yes	5/5	2/2
Geeta Gopalan (appointed 25 June 2015)	Yes	1/2[3]	–
Former Committee members			
Olivia Dickson (retired 31 December 2015)	Yes	4/5[3]	2/2

1 Number of meetings held during the period the member held office.
2 Apologies due to illness.
3 Conflict with an external appointment.

Chairman's overview

I am pleased to report that the Board Risk Committee fulfilled its responsibilities and met its key objectives during 2015. The annual effectiveness review concluded that the Committee continued to operate effectively.

Following a review of our corporate governance framework, the Balance Sheet and Board Risk Committees were merged to remove duplication in reporting and ensure more effective use of time. Responsibility for the oversight of balance sheet matters transferred to the Committee from July 2015. This report contains information relating to both Committees (for simplicity referred to as the "Committee") and I would like to thank Norman McLuskie for his chairmanship of the Balance Sheet Committee during the first half of the year.

The Committee maintained an appropriate balance, monitoring key risks whilst maintaining a dynamic approach, so that emerging risks were appropriately considered and management actions constructively challenged.

The Committee also continued to monitor the Group's risk management framework and the embedding of a suitable risk culture.

The Committee contributed to the oversight of key strategic programmes. This included the migration of the credit card business from MBNA and the launch of our new cards business. Further detail is set out in the case study on page 107.

Virgin Money continues to operate in a mature and increasingly competitive UK financial services market. In addition to UK macro economic and market risks the Committee considered the impact of geo-political uncertainty from other regions and ongoing changes in the regulatory environment (including the introduction of the Basel III Liquidity Coverage Ratio). The stress and scenario testing undertaken by management has given the Committee continued confidence in the Group's ability to mitigate these risks. Reverse stress testing was also undertaken to explore the vulnerabilities of the Group's strategies and plans and also to improve contingency planning.

Committee purpose and responsibilities

The purpose of the Committee is to monitor the Group's compliance with the Board's approved risk appetite, risk management framework and risk culture.

Examples of the way in which the Committee discharged its responsibilities during the year are set out below. Full details of the Committee's responsibilities are set out in

Corporate Governance Report

Board Risk Committee Report

the Committee terms of reference (these were updated in 2015 to include certain responsibilities of the Balance Sheet Committee) and can be found on our website at virginmoney.com/virgin/investor-relations.

Committee composition, skills and experience

During the year, the Committee welcomed Geeta Gopalan as a member on 25 June and Olivia Dickson retired as a member on 31 December. The Committee now comprises four Independent Non-Executive Directors who have a variety of industry backgrounds, including banking and financial services. The members of the Committee have a deep understanding of risk management and bring extensive experience and a broader perspective to the oversight of risk management. The Chair is also a member of the Audit Committee.

The Chairman, Chief Executive, CFO, Chief Risk Officer and Group Treasurer attend Committee meetings. The external auditor also attends most meetings.

How the Board Risk Committee spent its time in 2015

Set out below is a summary of the key matters considered by the Committee in 2015.

Risk appetite

The Committee considered the Group's risk appetite. In particular, the Committee:

- carried out the annual review of risk appetite alongside the strategic plan, to reflect the Group's latest commercial, economic and regulatory views, considering the statements and risk appetite metrics under each category of identified risk;
- received regular detailed risk reports analysing current and forecast performance against risk appetite metrics; and
- considered and challenged proposed changes to risk appetite measures and made appropriate recommendations to the Board.

Further details on the Group's risk appetite can be found in the Risk Management Report on page 140.

In November 2015, the Committee reviewed and recommended to the Board for approval the Risk Appetite Policy developed in line with Financial Stability Board Guidance.

Risk culture

The Committee is responsible for overseeing management's embedding of the risk culture and values throughout the Group. During the year, the Committee:

- supported policies, role profiles and training which ensured that there is clear understanding of expected behaviour and good practice; and
- received (ahead of the Remuneration Committee) reports from the Chief Risk Officer relating to executive incentive schemes and considered whether there were any performance issues or breaches that would require a risk adjustment to be made to the respective award. Further details on executive remuneration can be found in the Directors' Remuneration Report on pages 112 to 115.

Further details on the Group's risk culture can be found in the Risk Management Report on page 140.

Risk framework

The Committee has a key role in relation to the Group's risk management framework and during the year:

- reviewed new and material amendments to the Group's risk framework and policies recommended by the Chief Risk Officer;
- oversaw adherence to Group policies and standards and monitored any action taken resulting from material policy breaches; and
- received reporting on the Group's exposure to current and emerging risks as outlined by the framework.

In November 2015, the Committee conducted its annual review of the Group's risk management framework to ensure it remains robust and effective and concluded that it remains so. The review was undertaken as part of the risk review of the strategic plan and concluded that the risk management framework is effective in design and management of risk and supportive of strategy and risk appetite. Further details of the risk management framework can be found in the Risk Management Report on pages 148 to 149.

Board Risk Committee Report

Risk management

The Committee considered the Group's approach to risk management, and regulatory developments. In particular the Committee:

- reviewed the capability, resources, remit and authority levels of the risk function, and concluded that the risk function was adequately resourced and continued to be sufficiently independent with appropriate authority and standing within the Group;
- reviewed regular reports from the Chief Risk Officer summarising the main risks within the business, providing supporting quantitative data and additional commentary;
- reviewed regular reports from the Group Treasurer on matters relating to the management of the balance sheet;
- received reports and monitored the Group's approach to regulatory developments and the emerging macro economic and competitive landscape;
- reviewed and challenged management's development of scenario planning and stress testing as part of the regulatory capital requirements and preparation of the Recovery and Resolution Plan (RRP); and
- reviewed the Group's arrangements for detecting fraud and preventing bribery and concluded that all core elements of the anti-money laundering framework are in place and operating effectively.

More information on the Group's approach to risk management can be found on pages 140 to 149.

Credit Card migration

Background

In 2014, Virgin Money announced that it intended to grow the credit card book to £3 billion by 2018. In order to achieve this it developed a new credit card platform in partnership with leading system provider, TSYS, which allowed the Group to migrate its existing business to the new platform and originate new lending.

The safe migration of over 675,000 customer accounts to the new platform was a significant business change programme which had to be delivered within risk appetite, on time and with minimal customer and reputational impact.

Virgin Money began offering credit card products to the public using the new platform in February 2015, and by March 2015 had successfully migrated over 675,000 credit card customers from our existing administrator onto the new platform.

Board Risk Committee role

The Committee assisted the Board in overseeing the management of risks arising from the programme and ensured that independent risk oversight activity was completed, with regular reports on the status of this work and areas of challenge provided by the Chief Risk Officer.

- **Platform build** – Initial work to build the platform was heavily focused on credit and fraud risk management and included the creation of acquisition and behavioural scorecards as well as customer management and collection recovery strategies. Before switching to the new platform, risk oversight activity focused on evaluating the new system's security, performance and resilience. Work on financial crime prevention and detection arrangements included the validation of application fraud strategies, transactional alert systems and operational readiness. Reports were made to the Committee by the Chief Risk Officer to allow it to discharge its duty to monitor the operation of the Group within risk appetite.
- **Migration event planning** – In addition to comprehensive data mapping exercises, two full dress rehearsals were undertaken to validate the detailed migration plans. Findings from both events were incorporated into the plan for the live migration event. Senior management in risk conducted an independent scenario assessment looking at what could go wrong with the migration exercise. As a result of the scenario assessment, management put in place additional trained contact centre resource in anticipation of an increase in customer contact following migration. Reviewing the adequacy of contingency planning enabled the Committee to review and monitor the risk profile of the Group. The Group set aside a substantial amount of additional capital for the potential issues which may have arisen from the migration of credit card customers to the new platform and implementation of the platform build.
- **Migration event** – Members of the Risk Executive were on site throughout the migration event to assist when required. A 'command and control' structure was in place to ensure that the Executive were aware of, and able to respond to, issues as they arose.
- **Post implementation** – Monitoring of credit card business following migration was performed to ensure the prompt identification and resolution of issues, with routine reporting now embedded. 'Command and control' structures remained in place to ensure the appropriate escalation of issues. The Committee was regularly informed of issues and the actions to address them, enabling them to assess the adequacy of response.

Outcome

The Committee was satisfied that the key risk exposures were appropriately managed within risk appetite. Risk supported the business decision to go live with the migration and the activity completed successfully, with Virgin Money servicing all migrated customers from 23 March 2015.

Corporate Governance Report

Board Risk Committee Report

Significant risks considered by the Committee

Set out below are some of the significant risks facing the Group that were considered by the Committee in 2015. Further detail on the Group's principal risks can be found in the Risk Overview on pages 50 to 53.

Risks were carefully mitigated through rigorous risk and project management disciplines to ensure safe implementation.

Significant risks	Board Risk Committee review
Credit risk	The Committee monitored retail credit risk performance against the Group's risk appetite metrics and policies. The Committee considered the quality of lending and detailed reports on exposures to concentrated areas. These reviews led to the Committee approving changes to Group policy or risk appetite to reduce exposure in these regions.
Operational risks	The Committee received regular updates across operational risk including change programme management, incident management, outsourcing management and IT resilience including financial crime. The Committee monitors risks inherent with major outsource providers and received regular updates on their performance and resilience. The Committee continued to oversee the delivery of the Group information security programme to mitigate the threat of cyber attack. The Committee also received the annual report from the Money Laundering Reporting Officer which concluded that all core elements of Virgin Money's anti-money laundering framework are in place and operating effectively.
Conduct risk and compliance	The Committee received regular detailed updates from management on regulatory developments and upstream risk. The Committee assessed the impact of those developments on the Group's balance sheet, operational processes, systems and controls.
Funding and liquidity risk	The Committee reviewed and challenged the current and forecast funding and liquidity positions. The Committee considered reports on funding sources to ensure a prudent mix was maintained within risk appetite and policy limits. Balance sheet growth has been supported by the establishment of an MTN programme in April 2015. This enhanced the Group's funding mix to support growth and diversified its investor base.
Capital	The Committee monitored, reviewed and challenged management reports concerning the quality of the capital base and the forecast capital position considering the projected capital resources to ensure that the Group complies with current regulatory capital requirements and is well positioned to meet future requirements. The Committee also reviewed the results of the PRA UK Variant Stress Test scenarios published during the year. In addition, the Committee focused on specific scenarios designed by management.

Colin Keogh
Chair, Board Risk Committee

1 March 2016

Remuneration Committee Report

"We continue to strive to ensure that our remuneration policies and practices fairly reward our Directors and colleagues, support the delivery of the Group's strategy and the creation of shareholder value."

Marilyn Spearing
Chair, Remuneration Committee

Membership and meetings

	Independent	Meetings attended/ held in 2015[1]
Committee Chair		
Marilyn Spearing (appointed 1 January 2016)[2]	Yes	7 (7)
Committee members		
Norman McLuskie	Yes	7 (7)
Geeta Gopalan (appointed 25 June 2015)	Yes	2 (2)
Former Committee members		
Sir David Clementi (retired 21 May 2015)	No	4 (4)
Olivia Dickson (retired 31 December 2015)[3]	Yes	7 (7)

1 Number of meetings held during the period the member held office.

2 Ms Spearing was appointed as Chair of the Committee from 1 January 2016, having being a member since January 2014.

3 Mrs Dickson retired from the Board and as Chair of the Committee on 31 December 2015.

Chair's overview

I became Chair of the Remuneration Committee on 1 January 2016, following Olivia Dickson's retirement from the Board on 31 December 2015. On behalf of the Committee, I would like to thank Olivia for the contribution made with regard to remuneration matters in preparation for the Group's listing and first year as a listed company. I look forward to continuing to work with my colleagues during 2016.

I am pleased to report that good progress continues to be made on remuneration matters and their governance over the past year, despite the challenges of a continually changing regulatory environment. In my view, and as confirmed by the Board Effectiveness Evaluation, the Committee met its key objectives and carried out its responsibilities effectively.

2015 was a busy year for the Committee, as a result of a full remuneration agenda and the development of a robust reward framework in the form of the Directors' Remuneration Policy for 2015 and the Group-wide Internal Remuneration Policy for all colleagues. Both policies are designed to mitigate key regulatory and people risks associated with reward decisions and support sustainable growth, consistent with the risk appetite framework agreed with the Board.

We were delighted that 99.4% of our shareholders approved our first one-year Directors' Remuneration Policy, which was subject to a binding vote at our 2015 AGM. The implementation section of the Directors' Remuneration Report, along with the statement by the Chair of the Committee, also achieved an advisory 99.9% vote in favour. While the outcome of this resolution is not binding on the Group, it is of key importance to the Committee that its decisions are supported by the Group's shareholders. We look forward to presenting our new policy for approval at the 2016 AGM. If the new policy is approved, it will apply for a maximum of three years from the date of the AGM.

In January 2016 we consulted with a number of our major shareholders to gather their views on remuneration and, in particular, the key changes arising from the new policy. We also consulted with our main regulators, the FCA and PRA, throughout the year regarding our new policy. We are grateful for the supportive feedback we have received from all parties.

During 2015, the Committee has continued to strive to ensure that the remuneration policies and practices detailed in the Directors' Remuneration Policy and Directors' Remuneration Implementation Report fairly reward our Directors, support the delivery of the Group's strategy and the creation of shareholder value. As a result we hope you will support the resolutions relating to remuneration at the 2016 AGM.

The Committee dedicated significant time in 2015 and early 2016 to assessing the impact of ongoing changes to the regulatory environment concerning remuneration, in particular the implications of the PRA's deferral requirements on variable remuneration and considering the new European Banking Association (EBA) guidelines on sound remuneration policies issued in December 2015.

The Committee also approved the continued appointment of PwC as Committee advisers until the 2016 AGM, when PwC is to be put forward as the Group's new auditor. Subject to the shareholders approving the appointment of PwC, Deloitte will act from May 2016 as sole advisor to the Committee (in addition to its current role advising management). The Committee is comfortable that appropriate controls are in place to avoid any compromise to PwC's independence during this transitional period. The Committee would like to thank PwC for their significant contribution as remuneration advisers and for their consistently high standards of professionalism in executing this role.

Corporate Governance Report

Remuneration Committee Report

Committee purpose and responsibilities

The purpose of the Committee is to consider, agree and recommend to the Board an overall remuneration policy and philosophy for the Group that is aligned with the long-term interests of the Group. Full details of the Committee's responsibilities are set out in the Committee terms of reference (which were updated in February 2016) and can be found on our website at virginmoney.com/virgin/investor-relations.

Committee composition, skills and experience

The Committee comprises solely Independent Non-Executive Directors from a wide variety of backgrounds to provide a balanced and independent view on remuneration matters.

All Committee members have considerable experience in the financial services sector and a sound foundation in remuneration and risk governance. The Committee was pleased to welcome Geeta Gopalan as a member in June 2015. Geeta brings strong experience from her role on a variety of Boards in a wide range of sectors.

The Chairman, Chief Executive, HR Director, HR Director – Reward and Patrick McCall attend Committee meetings. Deloitte, who act as management's remuneration adviser and PwC, as the Committee's remuneration adviser, attend most Committee meetings.

How the Committee spent its time in 2015

An overview of how the Committee discharged its responsibilities and its key activities during the year can be found in the Committee Chair's Statement on page 111 and in the Implementation Report of the Directors' Remuneration Report on pages 122 to 123.

Marilyn Spearing
Chair, Remuneration Committee

1 March 2016

Directors' Remuneration Report

Statement by the Chair of the Remuneration Committee

Dear Shareholder,

On behalf of the Board and as Chair of the Remuneration Committee, I am pleased to present the Directors' Remuneration Report for the year ended 31 December 2015. I became Chair of the Virgin Money Remuneration Committee on 1 January 2016 having served as a member since 2014. I would like to thank my predecessor, Olivia Dickson, for her leadership of the Committee throughout 2015, the Group's first year as a listed company.

The Committee balances the views of our stakeholders with our duty to reward our Directors for their performance fairly, support the delivery of the Group's strategy and ensure that we are able to attract talented people. This statement and the accompanying report aim to demonstrate the context in which decisions have been made, the outcomes reached for the 2015 performance year and how the Committee intends to approach the year ahead.

2015

The Committee made significant progress on remuneration matters in our first full year as a listed company. Our 2015 Directors' Remuneration Policy was approved at the 2015 AGM with over 99.4% of shareholders voting in favour.

As outlined elsewhere in the annual report, 2015 has been a very successful year for Virgin Money and we continue to deliver strongly against our objectives. We have delivered growth and generated a significant increase in underlying profitability whilst maintaining our high-quality balance sheet.

These strong results translate to the Chief Executive being awarded a total bonus of 70% of fixed pay, which corresponds to 87.7% of the maximum bonus opportunity.

I am also pleased to report that upon the IPO anniversary an all colleague share award vested. These £1,000 awards were granted at the IPO price of £2.83 and vested at £3.57, giving each recipient Virgin Money shares worth £1,260.

Looking forward to 2016

In advance of the AGM the Remuneration Committee has undertaken a review of the Directors' Remuneration Policy to ensure it is aligned to the Group's business strategy and incentivises the delivery of our key strategic objectives. In conducting this review the Group's success since IPO, Prudential Regulation Authority (PRA) requirements relating to variable remuneration, and feedback from investors have all been taken into consideration.

As a result of the review the policy has been revised. The flexibility to employ a fixed allowance has been introduced. This is to ensure that total fixed remuneration remains competitive relative to market, whilst maintaining an appropriate balance of fixed pay to variable pay. It can also be employed to facilitate recruitment in the future if required. The variable pay focus has been changed to balance annual bonus and longer term incentive pay, accompanied by an extension in the overall deferral timelines for variable pay. In addition, to simplify variable pay, we are reducing the number of incentive plan measures.

We will continue to use financial and non-financial measures consistent with the Group's corporate objectives. This includes underlying Return on Tangible Equity (RoTE) which features in the annual bonus and Long Term Incentive Plan to reflect the importance of this measure as the company grows. We are on a journey where aligning bonus to RoTE will drive incremental steps to achieving a mid-teens RoTE over the longer term. Full details of the revised policy are set out within the following pages.

Chief Financial Officer

On 12 January 2016 it was announced that Peter Bole would join the Group as Chief Financial Officer. The remuneration arrangements for Mr Bole were in accordance with the policy previously approved by shareholders. It was necessary to buy-out a proportion of Mr Bole's share awards and bonuses from his previous employer and this is disclosed in the report.

During 2015, the Remuneration Committee also approved the terms that applied to Lee Rochford's departure. This was entirely consistent with the approved policy and full details are provided in this report.

Consideration of shareholders' views

Shareholders have a vital role in developing responsible pay practices. In January 2016, as part of our policy review, we engaged with a number of major shareholders to gather views and feedback in relation to our remuneration proposals.

I believe that the policy being proposed is in the interests of the Group and its shareholders. I am pleased to recommend it to you, along with the 2015 Implementation Report and this statement, ahead of the 2016 AGM.

Marilyn Spearing
Chair, Remuneration Committee
1 March 2016

Directors' Remuneration Report

Directors' Remuneration Policy

Directors' Remuneration Policy and Principles

The Group seeks to reward colleagues fairly for their contribution, whilst ensuring they are always motivated to deliver the best outcomes for stakeholders. To achieve this, colleagues are rewarded in line with UK listed financial services sector best practice, with no reward for inappropriate risk taking.

The Group's approach to remuneration for all colleagues, including Executive Directors, is designed to protect customers, corporate partners, shareholders and wider society and promotes the long term success of Virgin Money. It reflects the culture and supports the delivery of the business strategy:

- to maintain capacity for growth, Virgin Money ensures it remains competitive in the financial services market through regular market reviews. The Group's remuneration strategy aims to motivate individual out-performance against transparent and challenging objectives that are rigorously applied;
- to ensure a safe approach to remuneration, and in particular variable pay, clear risk principles are applied which aim to drive sustainable growth. Risk considerations are a material factor in the determination of pay. Malus adjustments and clawback apply to all variable pay;
- the Group aims to treat its colleagues in the same way that it serves customers – with honesty, transparency and fairness. Virgin Money believes in creating a culture where customer service is the priority. To achieve this, all colleagues receive an annual bonus opportunity, with no product-focused sales incentives in place. Balanced objectives are used to assess annual performance; and
- to ensure the approach to senior remuneration is fair, competitive and supportive of the Group's strategy, Virgin Money undertakes periodic reviews, at least annually. This also ensures that the Group's position remains appropriate relative to competitors.

Virgin Money aims to support colleagues and their families whilst enabling them to plan for the future through a competitive benefits package. The benefits package helps ensure low staff turnover, higher engagement and supports the Group's overall operational and financial efficiency.

Consideration of shareholders' and colleagues' views

At the AGM in May 2015, 99.4% of shareholders approved the first Directors' Remuneration Policy and the implementation section of the Directors' Remuneration Report achieved an advisory 99.9% vote in favour.

In January 2016 the Group engaged with a number of major shareholders to gather their views and feedback on the remuneration proposals. The policy set out in this section will apply, subject to shareholder approval at the 2016 AGM, from 1 January 2016.

Formal consultation on the remuneration of Executive Directors is not undertaken with colleagues. However, a colleague engagement survey is undertaken annually, including views on pay. Discussion on the Group's approach to remuneration and relevant colleague reward matters takes place with union representatives during the annual pay review cycle. The Remuneration Committee considers the overall pay review outcomes for colleagues when determining the salary for Executive Directors.

Remuneration Policy for Executive Directors

Base salary

Purpose and link to strategy	Base salary reflects the role of the individual taking account of responsibilities and experience.
Operation	Base salaries are normally reviewed annually. When determining and reviewing base salaries, the Committee considers: – corporate and individual performance; – the skills, experience and responsibilities of the Executive Director and their market value; – the scope and size of the role; – base salary increases for colleagues throughout the Group; and – external market factors. Base salaries from 1 January 2016 are detailed in the Implementation Report on page 124.
Maximum potential	Whilst there is no maximum base salary, any salary increases in percentage terms will normally be in line with increases awarded to other colleagues, but may be higher in certain circumstances. The circumstances may include but are not limited to: – where a new Executive Director has been appointed at a lower salary, higher increases may be awarded over an initial period as the Executive Director gains experience in the role; – where there has been an increase in the scope or responsibility of an Executive Director's role; or – where a salary has fallen significantly below market positioning given current size and scale of the Group. Base salary levels may be amended to take into account any regulatory changes.
Performance measures	N/A

Fixed Allowance

Purpose and link to strategy	To ensure that total fixed remuneration is commensurate with the role and to provide a competitive reward package for Executive Directors with an appropriate balance of fixed and variable remuneration. Also to facilitate recruitment of an Executive Director if required.
Operation	The Fixed Allowance will be delivered in cash and /or shares normally on a monthly basis. The Fixed Allowance is not pensionable.
Maximum potential	The maximum allowance is 100% of base salary.
Performance measures	N/A

Note: This component did not form part of the last approved remuneration policy, but is considered necessary to remain competitive in the market.

Pension

Purpose and link to strategy	To support the Executive Directors in building long-term retirement savings in a manner which does not expose the Group to any unacceptable financial risk.
Operation	Executive Directors are eligible to participate in the Group's defined contribution pension scheme. Alternatively, Virgin Money may make contributions to an Executive Director's personal pension arrangement. Only base salary is pensionable. An individual may elect, with the Group's consent, to receive some or all of their pension contribution as a cash allowance.
Maximum potential	The maximum allowance for Executive Directors is 30% of base salary.
Performance measures	N/A

Directors' Remuneration Report

Benefits

Purpose and link to strategy	To provide a competitive and cost effective flexible package delivered in a way which does not expose the Group to any unacceptable financial risk.
Operation	Virgin Money provides a range of benefits which may include private medical insurance, permanent health insurance and life assurance. The Committee retains the discretion to provide additional benefits as may be reasonably required. These may include national and international relocation benefits such as (but not limited to) accommodation, family relocation support and travel. The Executive Directors are entitled to a maximum of 30 days' holiday and any unused holiday may be bought back at the standard daily salary rate.
Maximum potential	The maximum value of benefits is based on the cost to the Group of providing each of the benefits in the 'Operation' section immediately above.
Performance measures	N/A

Annual Bonus and Deferred Bonus Share Plan

Purpose and link to strategy	The annual bonus is designed to reward performance, scored against annual weighted financial and non-financial measures.
Operation	Annual bonuses are discretionary and are based on Group and individual performance within the year. The determination of measures and their weighting are set annually and awards are determined by the Remuneration Committee at the end of the financial year. The Committee has discretion, in exceptional circumstances, to amend targets, measures, or number of shares under award if an event happens (for example a major transaction or capital raising) that in the opinion of the Committee, causes the annual targets or measures to no longer be appropriate or such adjustment to be reasonable. The Committee also has the discretion to reduce the vesting level of any award if it deems that the outcome is not consistent with performance delivered. The annual bonus may be delivered partly in cash and partly deferred into cash, shares or other instruments. The mechanism for making the bonus deferral is the Deferred Bonus Share Plan (DBSP). Deferral levels are set at the time of award and in line with regulatory requirements. At present this means that at least 60% of total variable pay is deferred, at least 50% of variable pay is paid in shares or other instruments, and vested shares (post taxation) are subject to a retention period. The deferral and holding periods may be amended to take into account any regulatory changes over the life of the policy. The Remuneration Committee may adjust awards or amend the terms of the awards in accordance with the DBSP rules. At the time of the shares being released and as long as this remains permissible under the regulatory rules, Executive Directors may receive an amount (in cash or in shares) equal to the dividends paid or payable between the date of grant and the vesting of the award on the number of shares which have vested. All awards will be subject to malus and clawback provisions (see page 120).
Maximum potential	The normal maximum bonus for Executive Directors is 100% of fixed pay. Under the DBSP rules, there is scope to award a bonus up to 300% of total fixed remuneration in exceptional circumstances, normally linked with recruitment. Any such Award would however remain subject to the overall regulatory rules.
Performance measures	Performance measures are determined by the Remuneration Committee each year. For 2016 these are set out in the Implementation Report on page 124. At least 50% of the annual bonus opportunity is based on performance against key financial measures determined at the beginning of each financial year. The remainder of the annual bonus is based on performance against non-financial measures, which will normally include a scorecard of brand, culture, control measures and personal strategic objectives.

Long Term Incentive Plan (LTIP)

Purpose and link to strategy	The plan is designed to reward delivery of the Group's strategy and growth in shareholder value over a multi-year period and aligns senior colleagues' interests with those of shareholders.
Operation	Awards are granted in the form of nil cost options or conditional shares, subject to performance conditions aligned to long term strategy. The Committee has discretion, in exceptional circumstances, to amend targets, measures, or number of shares under award if an event happens (for example a major transaction or capital raising) that in the opinion of the Committee, causes the targets or measures to no longer be appropriate or such adjustment to be reasonable. The Committee also has the discretion to reduce the vesting level of any award if it deems that the outcome is not consistent with performance delivered. Performance conditions will normally be tested over a period of three financial years. Deferral terms are set at the time of award and in line with regulatory requirements. Vested shares (post taxation) will be subject to a holding period. The performance, vesting and holding periods may be amended to take into account any regulatory changes over the life of the policy. At the time of the shares being released and as long as this remains permissible under regulatory rules, Executive Directors may receive an amount (in cash or in shares) equal to the dividends paid or payable between the date of grant and the vesting of the award on the number of shares which have vested. All awards will be subject to malus and clawback provisions (see page 120).
Maximum potential	The normal maximum award for Executive Directors is 100% of fixed pay. There is scope to increase Awards up to 300% of total fixed remuneration in exceptional circumstances, normally linked with recruitment. Any such award would remain subject to the overall regulatory rules.
Performance measures	Performance measures are determined by the Remuneration Committee each year. For 2016 these are set out in the Implementation Report on page 125.

Note: A change from the previously approved policy is to have a balanced ratio of annual bonus and LTIP rather than the previous 80:120 ratio. The Committee considers both components to be equally important having regard to longer deferral terms applying to annual bonus.

All-colleague plans

Purpose and link to strategy	If operated in the future, Executive Directors will be eligible to participate in HMRC approved all-colleague schemes which encourage share ownership, as approved by shareholders.
Operation	Executive Directors may participate in these plans if operated in the future in line with the prevailing HMRC guidelines (where relevant), on the same basis as other eligible employees.
Maximum potential	Participation levels will be in line with HMRC limits as amended from time to time.
Performance measures	N/A

Directors' Remuneration Report

Shareholding guidelines

Executive Directors are expected to hold a set percentage of salary in shares of Virgin Money, built up over five years from listing on 18 November 2014, or recruitment, whichever is the later.

	Requirement (% of salary)
Executive Directors	200%

The Chief Executive's standing against these guidelines is disclosed on page 131 of the Implementation Report.

Legacy awards and restrictions on payments

The Remuneration Committee reserves the right to honour any remuneration payments or awards and any payments or awards for loss of office, notwithstanding that they are not in line with the policy set out above where the terms of the payment or award were agreed before the policy came into effect (as set out in last year's Directors' Remuneration Policy or the Listing Prospectus where relevant). Such payments or awards are set out in the Implementation Report for the relevant year. This includes payments in relation to legacy deferred bonus awards and long term incentive awards and share options (including exceptional awards vesting on the listing of the Company) granted prior to listing of the Company.

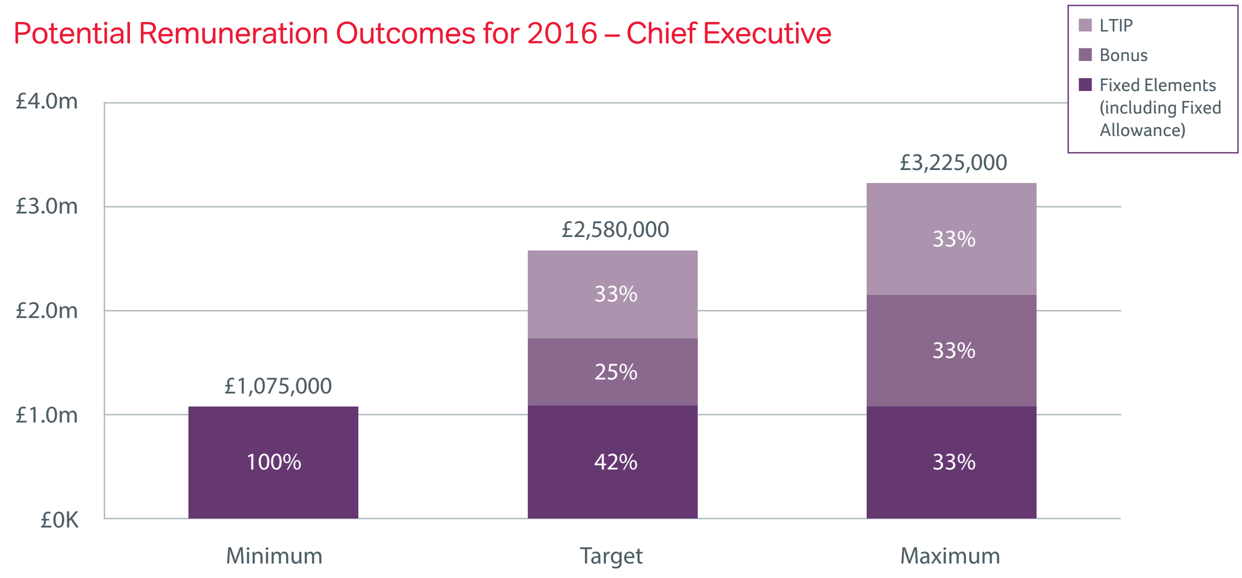
Illustration of application of Remuneration Policy

The chart on the following page illustrates the potential remuneration outcomes for the Chief Executive in 2016 in the following three scenarios:

- the minimum remuneration receivable, where only the fixed element is paid (salary, fixed allowance and pension);
- the target outcome is based on 60% of maximum annual bonus and 80% of maximum vesting under the 2016 LTIP award; and
- the maximum that may be paid, assuming maximum annual bonus opportunity is realised and full vesting of the 2016 LTIP award.

The amounts do not allow for share price appreciation and do not include any dividends or any payments in lieu of dividends. Salary figures are as at 1 January 2016 and assume the implementation of a fixed allowance of £100,000, a 2016 annual bonus (with a maximum award of 100% of fixed pay) and a LTIP award (with a maximum award of 100% of fixed pay).

Potential Remuneration Outcomes for 2016 – Chief Executive



Recruitment and appointment to the Board

In the event the Group appoints a new Executive Director, remuneration will be determined in line with the following principles:

- the Remuneration Committee will take into account all relevant factors, including the calibre and experience of the individual and the market from which they are recruited, whilst being mindful of the best interests of the Group and its shareholders and seeking not to pay more than is necessary;
- salary may be higher or lower than the previous incumbent but will be set taking into account the review principles set out in the policy table on page 113. Where appropriate, the salary may be set at an initially lower level with the intention of increasing salary at a higher than usual rate as the Executive Director gains experience in the role. For interim positions a cash supplement may be paid rather than salary (for example a Non-Executive Director taking on an Executive function on a short-term basis);
- a Fixed Allowance may be used to ensure that total fixed remuneration is commensurate with the role and competitive against the external market but with an appropriate balance of fixed and variable remuneration;
- so far as practical the Remuneration Committee will look to align the remuneration package for any new appointment with the Directors' Remuneration Policy on pages 113 to 115. The maximum variable pay opportunity would be within the regulatory requirements. This limit excludes any buy-out awards, which are governed as set out in the paragraph below;
- to facilitate recruitment the Remuneration Committee may need to 'buy-out' remuneration arrangements forfeited or forgone on leaving a previous employer, including long-term awards, deferred awards, in year and prior year annual bonuses and other contractual entitlements; and

Directors' Remuneration Report

- the value of the buy-out awards will broadly be the equivalent of, or less than, the value of the award being bought out. In accordance with regulatory requirements, these 'buy-out awards' will take into consideration relevant factors including, but not limited to:
  - the form of the award;
  - any performance conditions attached to those awards;
  - the vesting profile of the awards and the likelihood of vesting; and
  - relevant regulatory guidance in place in relation to buy-out awards.

Where a new Executive Director has to relocate to take up the appointment, either locally in the UK or from overseas, practical and/or financial support may be given in relation to relocation and mobility. This may include reimbursement of legal and accounting advice and tax equalisation payments.

Where an Executive Director is appointed from within the Group or following corporate activity or reorganisation (e.g. merger with another company), the normal policy would be to honour any legacy arrangements in line with the original terms and conditions.

Service Agreements

The notice period and date of the current Executive Director's service agreement is shown below:

	Notice period	Date of service agreement
Jayne-Anne Gadhia	12 months	18 November 2014

The Company policy is that Executive Directors are, and will be, employed on service agreements which include the following contractual provisions:

- the individual will be required to give 12 months' notice if they wish to leave the Group;
- the Group will give the individual 12 months' notice except where there is evidence of material misconduct or neglect or other circumstances where the individual may be summarily dismissed by written notice;
- the Group may require the Executive Director to take a period of garden leave for part or all of the notice period; and
- the Group has the discretion to terminate the individual's employment by paying the Executive Director in lieu of the notice period. The Group has the ability to make payments in equal monthly instalments and may stop or reduce such payments as appropriate if the Executive Director commences new employment.

The Company policy is that the Chairman will normally have a six month notice period, to be served by either party.

Termination payments

The impact of an Executive Director leaving the Group under various scenarios is summarised below. This reflects the service agreements and the relevant plan rules, and is the Remuneration Committee's policy in this area.

Remuneration element	Default position	Remuneration Committee discretion
Salary	Normally payable throughout notice period, subject to the duty to mitigate.	The Remuneration Committee could choose to use the payment in lieu of notice clause described on page 118 under 'Service Agreements'.
Fixed allowance	Normally payable throughout notice period, subject to the duty to mitigate.	The Remuneration Committee could choose to use the payment in lieu of notice clause described on page 118 under 'Service Agreements'.
Pension and other benefits	Pension allowance will normally be paid throughout the notice period. Non-cash benefits will continue to be provided during the notice period.	The Remuneration Committee may choose to pay cash compensation rather than continuing to provide a contractual non-cash benefit. This can include paying for accrued but unused holiday allowance.
Annual bonus	If the Executive Director is a good leaver then the Executive Director remains eligible to be paid a bonus. Annual bonuses are discretionary and would not usually be paid to a leaver mid-year. Leavers other than good leavers will not be entitled to an annual bonus in respect of the year of departure.	The Remuneration Committee will determine whether the Executive Director is a good leaver and the extent to which any bonus would be payable.
Deferred Bonus Share Plan	If the Executive Director is a good leaver then any outstanding Deferred Bonus Share Plan Awards will continue. Conditions will remain on the same terms and timing as with ongoing employment although a time pro-ration may apply. For leavers other than good leavers deferred bonuses will lapse.	The Remuneration Committee will determine whether the Executive Director is a good leaver. In the event of death, the Committee may allow the award to vest early in order for the estate to be wound up. The Remuneration Committee may determine the extent to which the application of the pro-rating principle applies.
LTIP	If the Executive Director is a good leaver then any outstanding LTIP awards will continue. Conditions will remain on the same terms (both in respect of timing and performance conditions) and a time pro-ration shall apply. For leavers other than good leavers the LTIP awards will lapse.	The Remuneration Committee will determine whether the Executive Director is a good leaver, the extent to which the performance condition is met at the end of the normal performance period and the application of the time pro-rating principle. In the event of death, the Committee may allow the award to vest early in order for the estate to be wound up.
Legacy awards	These consist of the IPO Incentive Plan, the FY12 and FY13 deferred bonuses, the former Chief Financial Officer's buy-out award. If the Executive Director is a good leaver then the entitlement to any awards will continue, but vesting will remain on the same terms consistent with ongoing employment. For leavers other than good leavers, awards will lapse.	The Remuneration Committee will determine whether the Executive Director is a good leaver. In the event of death, the Committee may allow the award to vest early in order for the estate to be wound up.
Chairman and Non-Executive Directors' fees	No compensation is payable in the event of early termination apart from the notice period.	None.

Directors' Remuneration Report

The Remuneration Committee will determine, at its absolute discretion, whether an Executive Director is a good leaver by virtue of their employment ending due to injury, ill-health, disability, redundancy, retirement, death, or any other reason (except for dishonesty, fraud, misconduct or any other circumstances justifying summary dismissal) as determined by the Remuneration Committee. The Remuneration Committee reserves the right to make additional termination payments where such payments are made in good faith in discharge of an existing legal obligation (or by way of damages for breach of such an obligation), or by way of settlement or compromise of any claim arising in connection with the termination of an Executive Directors' office or employment.

Takeover

In the event of a takeover or other major corporate event (but not an internal reorganisation of the Group) all outstanding awards granted under the Group's share plans would vest on the date of that event, subject to relevant regulation. For the LTIP the Remuneration Committee will determine the extent to which the performance conditions have been met and the extent to which the time pro-rating principle should be applied.

None of the Executive Directors have any special contractual employment terms related to a takeover which would enhance their position or trigger additional payments.

Malus and clawback

In the interests of sound risk management for the benefit of the Group, and to ensure compliance with regulatory obligations, all variable remuneration is subject to malus and clawback provisions. These conditions are set out in the service agreements for Executive Directors, as well as the DBSP and LTIP rules.

A performance adjustment may include, but is not limited to:

- reducing a colleague's bonus outcome for the current year;
- reducing the amount of any unvested deferred variable remuneration (including LTIP awards) to which a colleague is entitled (malus);
- requiring repayment (clawback) on demand (on a net basis) of any cash and share awards received at any time during the seven year period after the date of award ('the Clawback Period') which may be extended by a further three years where required; and
- requiring a bonus which has been awarded (but not yet paid) to be forfeited.

In the case of Group-wide adjustment, measures may also include:

- reducing the overall annual bonus pool; and/or
- reducing the overall unvested or unpaid awards.

The following non-exhaustive list outlines the circumstances in which malus and/or clawback measures could be triggered:

- where a colleague has participated in or was responsible for conduct which resulted in significant losses to the Group, as determined by the Remuneration Committee;
- where a colleague has significantly failed to meet appropriate standards of fitness and propriety, taking into account their seniority, experience, remuneration and level of responsibility;
- where the Group or the relevant business unit has suffered a material failure of risk management;
- where the Group has reasonable evidence of fraud or material dishonesty by the colleague;
- where the Group becomes aware of any material wrongdoing on the part of the colleague that would have resulted in the relevant award not being made had it known about such material wrongdoing at the time the relevant award was made;
- where the Group becomes aware of a material error in assessing the colleague's performance against the relevant performance conditions at the time the award was made; and
- the colleague has acted in any manner which, in the opinion of the Remuneration Committee, has brought or is likely to bring the Group into material disrepute or is materially adverse to the interests of the Company.

Colleague remuneration and engagement

When reviewing and setting Executive Director remuneration, the Remuneration Committee takes into account the pay and employment conditions of all colleagues. Specifically, the level of any Group-wide pay review is a key determinant when setting the level of any increase to Executive Directors' salaries. Colleague engagement is a measure within the scorecards for both the annual bonus and the LTIP.

There is no colleague representative on the Remuneration Committee. Instead, time is taken to meet and listen to the views of many colleagues. One of the duties of the HR Director is to brief the Board on colleague views and, as a regular invitee to Remuneration Committee meetings, he ensures that decisions are made with appropriate insight to colleagues' views.

The structure of the Executive Directors' remuneration packages cascades down to other colleagues. Particular points to note are:

- LTIP awards are granted to the wider Virgin Money Executive Team, with the same variable pay structure and performance conditions;
- all colleagues are eligible to participate in an annual bonus arrangement, with no product-focused sales incentives. Instead, all bonuses are subject to a balanced scorecard of measures with particular emphasis on customer experience; and
- colleagues in certain roles may receive a fixed allowance where this is considered appropriate taking into account pre-determined criteria.

On listing, the Board granted all eligible colleagues an award over £1,000 worth of Virgin Money shares (353 shares each). These shares vested on 18 November 2015, the first anniversary of listing. As at 31 December 2015 over 70% of colleagues are shareholders in the Company.

Chairman and Non-Executive Directors

The table below sets out the Remuneration Policy which will apply, subject to shareholder approval at the 2016 AGM, to the Chairman and Non-Executive Directors from 1 January 2016.

Chairman and Non-Executive Director Fees

Purpose and link to strategy	To ensure the Group is able to engage and retain highly skilled and experienced individuals who can provide a valuable contribution, having a significant range and depth of expertise.
Operation	Fees payable to the Chairman are determined by the Remuneration Committee, whilst the fees paid to the Non-Executive Directors are set by the Board. The Board undertakes periodic reviews, at least annually, of Non-Executive Director fees and this may lead to fee increases. The fees are set at a rate that reflects the individuals' experience, value to the Group and the expected time commitment of them. The regulatory regime and the practical aspects of running a complex financial services company are important inputs to remuneration decisions. For the Non-Executive Directors, there is a base fee which is then supplemented by additional fees in respect of chairing and being a member of Board committees. Incremental fees will be paid for additional duties and time commitment, such as those of the Senior Independent Director. The current fees are set out on page 125. From time to time, new Board Committees may be established and/or responsibilities distributed between Committees, at which point fees for Committee membership and Chairmanship may be reviewed. The Chairman and Non-Executive Directors are reimbursed for expenses (grossed-up where taxable) incurred in performing their duties. For individuals based outside of the UK this will include travel to and from the UK. The Chairman has access to a vehicle for personal use, which is a taxable benefit, and may be offered access to private medical insurance.
Maximum limit	The maximum aggregate value of fees payable to the Chairman and the Non-Executive Directors is capped at £2 million under the Articles of Association.
Performance metrics	No remuneration payable to the Chairman and the Non-Executive Directors has performance conditions.

Directors' Remuneration Report

Implementation Report

Purpose and membership of the Remuneration Committee

The role of the Remuneration Committee is to determine and recommend to the Board a fair and responsive remuneration framework to ensure that the Group's most senior Executives are appropriately rewarded and incentivised for their contribution to the Group's performance. The Remuneration Committee's primary purpose is to formulate policies that ensure a clear link between reward and performance and are compliant with regulatory requirements.

Remuneration Committee membership in 2015

Marilyn Spearing	Member since 29 January 2014 (and Chair from 1 January 2016)
Norman McLuskie	Member since 27 January 2010
Geeta Gopalan	Member since 25 June 2015
Olivia Dickson	Member from 1 September 2014, Chair from 5 September 2014 to 31 December 2015, on which date she retired from the Committee
Sir David Clementi	Member from 7 October 2011 to 21 May 2015, on which date he retired from the Committee.

Other attendees (by invitation from time to time) included: Glen Moreno, Patrick McCall, Jayne-Anne Gadhia, Matt Elliott (HR Director), and Simon Leeming (HR Director – Reward). To manage potential conflicts of interest, those five individuals did not attend at times when their own remuneration outcome was discussed and approved. PwC (the Committee's independent consultants in relation to Directors' remuneration) and Deloitte also attended meetings where invited. The Company Secretary attended meetings to record minutes.

Remuneration Committee activity in 2015

There were 7 meetings of the Remuneration Committee during 2015. The key matters were as follows:

Date	Pay / bonus	Policy / Governance
Q1	– FY14 pay and bonus outcomes – Performance conditions for the FY15 Annual Bonus and LTIP – Release of deferred bonus awards	– Directors' Remuneration Policy for FY15 – FY14 Directors' Remuneration Report – FY14 PRA Remuneration Policy Statement – Review of the Company-wide remuneration policy for 2015
Q2	– Personal strategic objectives for Executive Directors for the FY15 annual bonus	– Company-wide remuneration policy for 2015 – Code Staff population for 2015 – Review of EBA consultation on sound remuneration practices. – Review of deferral implications of the new Remuneration Code as introduced under PRA Policy Statement PS12/15
Q3	– Terms for the outgoing CFO – Release of historic deferred bonuses	
Q4	– Review the design of the FY16 Annual Bonus and LTIP – Release of Executive awards vesting under the IPO Incentive scheme	– Review the performance measures for the FY16 Annual Bonus and LTIP

Advisors to the Remuneration Committee

During 2015, the Remuneration Committee took external advice from PwC, the Committee's independent consultants in relation to Directors' remuneration.

PwC is a member of the Remuneration Consultants Group and complies with the professional body's code of conduct. This supports the Remuneration Committee's view that the advice received was objective and independent. PwC's fees for 2015 amounted to £182,697. During the year, PwC also provided advice on an internal audit contract, Treasury systems, payroll tax, IFRS 9 and VAT.

The Committee approved the continued appointment of PwC as Committee advisers until the 2016 AGM, when PwC are to be put forward as the Group's new auditor. Subject to the shareholders approving the appointment of PwC as Group auditor, Deloitte will act from May 2016 as advisor to the Committee (in addition to their current role advising management). The Committee is comfortable that appropriate controls are in place to avoid any compromise to PwC's independence during this transitional period.

Statement of voting at Annual General Meeting

The proposals on the Group's remuneration policy and the remuneration offered to the Executive Directors in 2015 were detailed within the Directors' remuneration report for 2014 and were voted on at the 2015 AGM. The shareholder votes submitted at the meeting, either directly, by mail or by proxy, were as follows:

	Votes in favour		Votes against		Votes withheld
	Number of shares	Percentage of votes cast	Number of shares	Percentage of votes cast	Number of shares
Remuneration Policy	374,092,808	99.43%	2,148,264	0.57%	473,652
Remuneration Implementation Report	375,710,730	99.86%	513,649	0.14%	490,100

Directors' Remuneration Report

Implementation of the policy in 2016

The following sets out how the Directors' Remuneration Policy will be applied in 2016:

Fixed Pay

Base salary	Jayne-Anne Gadhia (Chief Executive): £750,000
Fixed Allowance (subject to shareholder approval)	Jayne-Anne Gadhia (Chief Executive): £100,000
Pension and other benefits	No change from the stated policy.

Annual Bonus

Opportunity	Maximum annual bonus opportunity is 100% of fixed pay for Executive Directors.
Deferral terms	For 2016: – up to 32% of any bonus will be paid in cash following the publication of the financial statements for the previous year; – up to 32% of any annual bonus will be converted into an award of equivalent value under the Deferred Bonus Share Plan, vesting immediately on award and the resultant number of shares (post taxation) will be subject to a six month retention period; – up to 36% of any bonus will be converted to an award of equivalent value under the Deferred Bonus Share Plan, vesting equally from the third anniversary to the seventh anniversary and the resultant number of shares (post taxation) will be subject to a six month retention period; At the time of the shares being released Executive Directors may receive an amount (in cash or shares) equal to the dividends paid or payable between the date of grant and the vesting of the award on the number of shares which have vested.
Performance measures and targets	The Remuneration Committee has determined that for 2016 the annual bonus will be based on: – financial measures (underlying profit before tax, cost of risk, underlying return on tangible equity) – 60% weighting – non-financial measures (personal strategic objectives and a series of brand, culture and control measures) – 40% weighting The Board considers the targets that apply to these measures to be commercially sensitive at this time but will provide information on the level of payout relative to the performance achieved in next year's Implementation Report. The Remuneration Committee has determined that 60% vesting is justified for target performance and 0% is justified for threshold performance.

Long Term Incentive Plan

Opportunity	LTIP awards in 2016 will be granted to Executive Directors over shares worth 100% of fixed pay.
Vesting terms	The performance period will be the three years commencing on 1 January 2016. The intended date of grant is March 2016. To the extent that the performance measures are satisfied, awards will vest equally from the fourth anniversary of the date of grant to the eighth such anniversary. At each vesting date the resultant number of shares (post taxation) will be subject to a six month retention period.
Performance measures and targets	The Remuneration Committee has chosen performance measures that are based on delivering the Company's strategic objectives, and the continued creation of shareholder value. This choice and the calibration of the targets is consistent with the strategic plan. The Remuneration Committee has determined that 80% vesting is justified for target performance and 20% is justified for threshold performance. Performance against the targets will be subject to a risk assessment review. The following table outlines the weightings and measures for the 2016 awards.

Measure	Target	Weighting
Underlying Earnings Per Share	Threshold: 15% p.a. Target: 20% p.a. Maximum: 25% p.a.	30%
Underlying Cost: Income Ratio	Threshold: 50% Target: 47.5% Maximum: 45%	20%
Underlying return on tangible equity	Threshold: 13.5% Target: 15.0% Maximum: 16.5%	30%
Scorecard of measures relative to external comparators and internal scores	a) Customers b) Colleagues c) Conduct Risk	20%

Outcomes will be disclosed on a retrospective basis after the end of the three year performance period.

Chairman and Non-Executive Director fees in 2016

A review of Non-Executive Director fees was carried out in early 2016. Recognising that Non-Executive responsibilities continue to increase significantly in an evolving regulatory environment, the Committee Chairmanship and Committee Membership fees have increased with effect from 1 February 2016. The changes are reflected in the table below alongside the new Senior Independent Directorship fee and the other fees which remain unchanged from 2015.

2016 fee policy	2016	2015
Chairman fee[1]	**£350,000**	£350,000
Non-Executive Director basic fee	**£80,000**	£80,000
Senior Independent Directorship[2]	**£20,000**	£–
Audit Committee Chairmanship	**£25,000**	£20,000
Remuneration Committee Chairmanship	**£25,000**	£20,000
Board Risk Committee Chairmanship	**£25,000**	£20,000
Nomination Committee Chairmanship	**£–**	£–
Audit Committee Membership	**£10,000**	£7,500
Remuneration Committee Membership	**£10,000**	£7,500
Board Risk Committee Membership	**£10,000**	£7,500
Nomination Committee Membership	**£–**	£–

1 The Chairman has access to a vehicle for personal use, which is a taxable benefit, and is offered access to the Group's private medical insurance scheme which he has accepted and chosen to personally fund.

2 Subject to shareholder approval, implementation to be applied from 1 February 2016.

Non-Executive Directors may receive more than one of the above fees.

Directors' Remuneration Report

Remuneration outcome for 2015

Executive Directors (audited)

The following table summarises the total remuneration awarded in relation to Executive Director services during 2015.

	Jayne-Anne Gadhia		Lee Rochford	
	2015 £'000	2014 £'000	**2015[1] £'000**	2014 £'000
Salary	**725**	648	**317**	453
Taxable benefits[2]	**8**	8	**–**	–
Pension allowance[3]	**218**	139	**48**	68
Total fixed	**951**	**795**	**365**	**521**
Bonus	**666**	1,510	**147**	852
LTIP and legacy awards	**–**	1,342[4]	**–**	889[4]
Total remuneration	**1,617**	**3,647**	**512**	**2,262**
Additional disclosure: Fixed pay and annual and deferred incentives for 2015				
Total remuneration	**1,617**	**3,647**	**512**	**2,262**
Less: IPO incentive	**–**	**(1,342)**	**–**	**(889)**
Fixed pay and annual and deferred incentives for 2015	**1,617**	**2,305**	**512**	**1,373**

1 Mr Rochford stepped down as an Executive Director on 31 August 2015. The figures shown above for salary, pension and benefits are for the period 1 January 2015 to 31 August 2015. In addition, Mr Rochford is entitled to salary (at the rate of £475,000 per annum), pension (£72,500 per annum) and benefits for the period 1 September 2015 to date of termination of his employment (no later than 31 August 2016). A further amount of up to £12,000 will be payable to Mr Rochford relating to legal fees. In respect of the 2015 bonus, the Remuneration Committee assessed performance against the relevant performance measures and pro-rated for time served.

2 Taxable benefits comprise car allowance and private medical insurance.

3 The directors have no prospective right to a defined benefit pension as a result of 2015 qualifying service.

4 Represents the full value of IPO Incentive award based on the value of the award at the time of vesting (details on page 132).

The following table summarises the fixed pay and annual and deferred incentives for 2015.

	Jayne-Anne Gadhia		Lee Rochford	
	2015 £'000	2014 £'000	**2015 £'000**	2014 £'000
Cash[1]	**1,184**	1,097	**431**	692
Deferred[2]	**433**	1,208	**81**	681
Sub-total	**1,617**	2,305	**512**	1,373
LTIP[3]	**–**	–	**–**	–
Total	**1,617**	**2,305**	**512**	**1,373**

1 Represents total fixed pay and the proportion of annual bonus paid in cash in March following the performance year.

2 Represents the proportion of annual bonus which is awarded under the Deferred Bonus Share Plan.

3 The value of awards made under the LTIP will appear in the total remuneration table in the year of vesting.

Variable Awards

Annual Bonus

For 2015 the Chief Executive had a maximum annual bonus opportunity of 80% of fixed pay. For the former Chief Financial Officer the maximum was 80% of salary.

For each Executive Director, the 2015 annual bonus determination was based on performance against:

- financial measures (60% of overall award): underlying profit before tax, underlying return on tangible equity, underlying cost:income ratio and capital ratio;
- brand, culture, control objectives (20% of overall award): based on performance against objectives from the Group's corporate scorecard; and
- personal strategic objectives (20% of overall award): based on performance against pre-determined personal strategic objectives.

Actual performance against the 2015 bonus targets was as follows:

					Chief Executive	
Performance measure	**Threshold (0%)**	**Target (60%)**	**Maximum (100%)**	**Actual performance[1]**	**Weighting at maximum**	**Bonus score**
Underlying PBT	**£142.5m**	**£158.3m**	**£174.1m**	**£172.8m**	20%	19.3%
Underlying cost:income ratio	**64.9%**	**62.5%**	**60.1%**	**61.2%**	15%	12.3%
Underlying return on tangible equity	**8.4%**	**9.6%**	**10.5%**	**10.9%**	15%	15.0%
CET1 capital ratio	**<16.0% or >18.0%**	**16.0% to 16.5% or 17.5% to 18.0%**	**>16.5% and <17.5%**	**17.5%**	10%	6.0%
Brand, culture, control				**as explained below**	20%	17.0%
Personal strategic objectives				**as explained below**	20%	18.0%
Total bonus					**100%**	**87.7%**
						70% of fixed pay

1 The FSCS Levy was previously excluded from underlying performance measures but it is now included as it is considered to be a recurring cost to the Group however for FY15 bonus performance measures have not been adjusted to reflect this change and outcomes are reported in the table above excluding the FSCS Levy.

Brand, Culture, Control (20% weighting)

- Improved Customer Net Promoter Scores while growing customer base to over 3 million.
- Ongoing development of unique 'everyone's better off' culture demonstrated through top quartile colleague engagement scores.
- Enhanced levels of donations made via Virgin Money Giving.
- Prudential risk approach has driven high quality of credit compared with the industry average.

Final outcome: 17% out of a maximum 20%

Personal strategic objectives (20% weighting) – Chief Executive

- Experienced executive team in place with a new structure and appointments made.
- Successful migration of 675,000 Credit Card customers with no material customer detriment.
- Successful transition of the Company into public life, including delivery of annual and interim results and implementation of dividend policy (with the first dividend payment delivered in October 2015).
- Successful launch of the Virgin Money Foundation, with inaugural grant applications totalling £8m.
- Developed next phase strategy for Virgin Money.

Final outcome: 18% out of a maximum 20%

Directors' Remuneration Report

The bonus awarded to the Chief Executive is summarised in the table below:

Name	Jayne-Anne Gadhia
Maximum opportunity (% of fixed pay)	80%
% of fixed pay awarded for 2015	70%
Bonus awarded for 2015	£666,500

For the 2015 annual bonus, 35% of the annual bonus will be paid in cash in March 2016, 35% will be paid in shares with a six-month holding period. The remaining 30% will be deferred with one third vesting in March 2017, one third vesting in March 2018 and the remaining one third vesting in March 2019 (each with a six month holding period). Once vested, the awards remain subject to clawback provisions, in line with the Group policy.

LTIP

FY15 LTIP awards were made in March 2015 (120% of fixed pay for the Chief Executive and 120% of salary for the former Chief Financial Officer) and will be assessed against performance at 31 December 2017 based on the performance conditions set out in detail in the 2014 Directors' Remuneration Report. One-third of the award will vest after three years in March 2018, one-third after four years in March 2019 and the final one-third after five years in March 2020 (each with a six month holding period). Once vested, the awards remain subject to clawback provisions, in line with the Group policy.

Former Chief Financial Officer

Lee Rochford stepped down as Chief Financial Officer (CFO) and as an Executive Director on 31 August 2015. In accordance with the terms of his service agreement and the Group's remuneration policy, Mr Rochford will continue to receive salary, pension allowance and other benefits until the end of his notice period on 31 August 2016 (unless the termination date is brought forward by Mr Rochford, with the agreement of Virgin Money). In the event of an earlier termination date, payments in respect of salary, pension allowance and other benefits will only be made up to the termination date.

The Remuneration Committee determined that Mr Rochford would retain previous awards as set out in the Group's Annual Report and Accounts for 2014, together with an award over 52,094 shares granted under the 2015 Long Term Incentive Plan (which has been time pro-rated and will remain subject to the pre-vesting performance conditions) and a deferred award over 51,614 shares in respect of the 2014 annual bonus (also pro-rated for time served) which will be released on the previously set dates.

The Remuneration Committee also determined that Mr Rochford would remain eligible to be considered for a pro-rated 2015 annual bonus award for time in role as CFO. The Remuneration Committee assessed the relevant performance measures relating to the 2015 annual bonus and determined that the Financial and Brand, Culture and Control measures will apply in line with the table on page 127. Given that Mr Rochford stepped down from the role of CFO in August 2015, there was limited ability to meet the personal strategic objectives in full and therefore an outcome of 5% out of a maximum of 20% was determined. The overall outcome has been pro-rated for time served in 2015. Applying these outcomes, the total bonus awarded to Mr Rochford in respect of 2015 (before deferral) was £189,500. In line with the deferral terms, 35% of the annual bonus will be paid in cash in March 2016, 35% will be paid in shares with a six-month holding period. The remaining 30% will be deferred and subject to additional pro-ration for time served, with one third vesting in March 2017, one third vesting in March 2018 and the remaining one third vesting in March 2019 (each with a six month holding period). The consequence of the additional pro-ration applicable to the deferred element of the total bonus is that the maximum bonus payable to Mr Rochford is £147,126 (which could be reduced if the termination date is brought forward). This is the figure included in the Remuneration outcome for 2015 table on page 126. Once vested, the awards remain subject to clawback provisions, in line with the Group policy.

Appointment of Chief Financial Officer

On 12 January 2016 it was announced that Peter Bole would be joining as the new CFO at a date to be confirmed. Mr Bole will be paid an annual base salary of £500,000. In addition he will receive pension contributions of 20% of base salary, life assurance, permanent health insurance and private medical insurance. He will be eligible to receive an annual bonus and an annual award under the Virgin Money Long Term Incentive Plan, which together will not exceed 200% of fixed pay. Mr Bole will also receive one-off awards to compensate for remuneration forfeited as a result of leaving his current employer's share incentive arrangements. On joining Mr Bole will receive (i) an award of Virgin Money shares with a value of £653,873, which is not subject to performance conditions; and (ii) an award of Virgin Money shares with a value of £472,914, subject to Virgin Money performance conditions. Both of these awards will vest in line with Mr Bole's forfeited awards from his current employer. Mr Bole will also receive a one-off award to compensate for remuneration which he may forfeit in 2015/16 as a result of leaving his current employer, up to a maximum of £749,000. The final amount and terms of the award will be disclosed once awarded.

Percentage change in remuneration of Chief Executive versus the wider employee population

Figures for 'All Colleagues' are calculated using salary figures for all relevant colleagues except the Chief Executive, which is considered to be the most appropriate group of colleagues for these purposes.

	% change in base salary	% change in annual bonus (2014-2015)[2]	% change in taxable benefits (2014-2015)
Chief Executive	11.8%[1]	-55.9%	0%
All Colleagues	3.5%	5.2%	0%

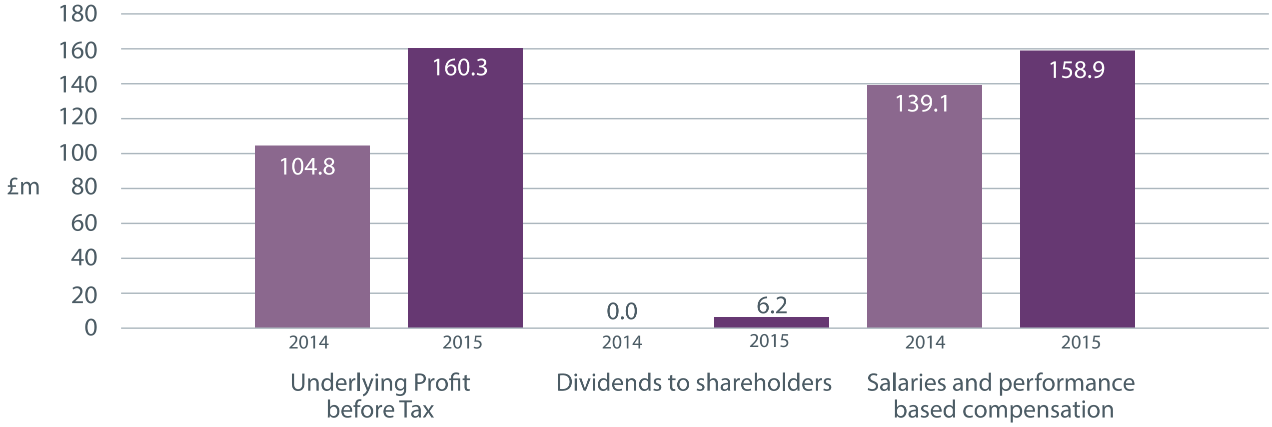
Note the percentages for "All Colleagues" included in the table above represent the year end position as at 31 December 2015 compared with the year end position as at 31 December 2014. The percentages are adjusted for movements in colleague numbers and other impacts to ensure a like for like comparison.

1 The percentage change for the Chief Executive's salary represents the difference between the salary included in the single figure table on page 126 with the corresponding figure in 2014. As reported in the 2014 Directors' Remuneration Report, the Chief Executive's salary increased on listing (November 2014) to reflect the associated additional responsibility and duties on leading a publicly listed company but did not change as part of the overall 2014/15 pay review. From 1st January 2016, following the overall 2015/16 pay review, the Chief Executive's salary will be £750,000.

2 This figure represents the percentage change in the FY15 Annual Bonus when compared with the FY14 Annual Bonus. In the case of the Chief Executive, this comparison disregards awards made related to FY15 under the Long Term Incentive Plan.

Relative spend on pay

A year on year comparison of the relative spend on pay is shown below. Underlying profit before tax has been used for comparison on the basis that it reflects performance, excluding one-off events. Total spend on salaries and performance based compensation in 2015 increased by 14% against an increase in underlying profit before tax of 53%. Note the Group distributed its first dividend payment to shareholders in October 2015.



Directors' Remuneration Report

Payments within the reporting year to past Directors (audited)

Finlay Williamson ceased to be an Executive Director on 7 October 2013. He left the Company's employment in September 2014 as a good leaver. As part of arrangements on leaving the Company, a deferred bonus payment of £17,434 was released to Mr Williamson during 2015.

Chairman and Non-Executive Directors' fees (audited)

	Fees paid in 2015 (£000s)	Fees paid in 2014 (£000s)
Glen Moreno	**253[1]**	–
Sir David Clementi (until 30/6/15)	**496[2]**	515[2]
Colin Keogh	**111**	169[3]
Norman McLuskie	**125**	174[3]
Olivia Dickson (from 01/09/14 until 31/12/15)	**111**	88[3]
Marilyn Spearing	**106**	160[3]
James Lockhart III (until 11/9/15)	**56**	95
Patrick McCall	**80**	95
Gordon McCallum	**80**	95
Geeta Gopalan (from 25/6/15)	**53**	–

1 Glen Moreno has access to a vehicle for personal use, which is a taxable benefit.

2 The fee for 2014 and 2015 includes £540,000 paid in nine monthly instalments commencing in October 2014 and concluding in 30 June 2015. In addition, Sir David Clementi agreed to waive his annual fee for the period 21 May 2015 to 30 June 2015, to reflect the appointment of Glen Moreno as Chairman from 21 May 2015. This was disclosed in the Listing Prospectus and the 2014 Directors' Remuneration Report.

3 Each of the independent Non-Executive Directors received a one-off additional fee of £50,000 during 2014 to reflect the additional time commitment associated with the listing of the Company. This was disclosed in the Listing Prospectus and the 2014 Directors' Remuneration Report.

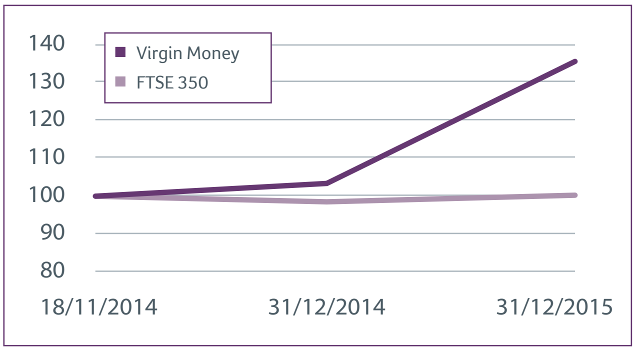
Breakdown of Non-Executive Directors' fees

Non-Executive Directors receive specific committee fees, as set out in the table on page 125. There were no changes to fees during 2015.

Historical TSR performance and Chief Executive pay

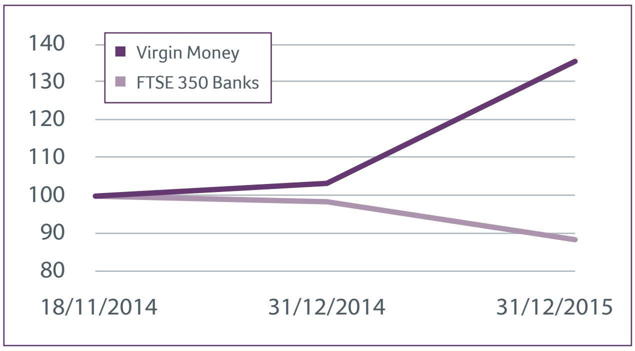
The graph below shows the total shareholder return (TSR) of the Company for the period from the date when shares were listed on the London Stock Exchange (18 November 2014) to the end of the 2015 financial year, and the performance of the FTSE 350 Index of the same time period. As a recently listed company, a five year TSR graph cannot be included. The FTSE 350 Index has been chosen as the comparative broad equity index because the Company is a member.

Virgin Money TSR v FTSE 350



For further context and comparison to some competitors, the graph below shows the Company's TSR performance against the FTSE 350 Banks Index over the same period.

Virgin Money TSR v FTSE 350 Banks



Chief Executive remuneration outcome – historic (since Initial Public Offering)

Financial year ending	31/12/2015	31/12/2014
Chief Executive	**Jayne-Anne Gadhia**	Jayne-Anne Gadhia
Total remuneration single figure (£000)	**1,617**	3,647
Annual bonus awarded (% of maximum opportunity)	**87.7%**	95%
Long term Incentive Award vesting	**–**	–

Outstanding share awards

Directors' interests (audited)

The table below summarises the Executive Directors' shareholdings and share interests.

		Number of shares		
	Owned outright	Unvested (not subject to performance conditions)	Unvested (subject to performance to conditions)	Total
Jayne-Anne Gadhia	**2,242,251**	**976,793**	**278,875**	**3,497,919**
Former Directors who served in 2015 (shareholding at date stepped down from Board)				
Lee Rochford	**207,847**	**356,912**	**52,094**	**616,853**

Shareholding guidelines

Executive Directors are expected to hold 200% of salary in shares of Virgin Money built up over five years from listing or recruitment, whichever is the later.

As a result of the shareholdings in the table on page 134, the position for the Executive Directors in 2015 is as follows:

		Shareholding requirement		Current shareholding[1]		
Executive Directors	Base salary	% of base salary	Number of shares (at 31.12.15 closing price of £3.80)	% of base salary (at 31.12.15 closing price of £3.80)	Value of shares held (at 31.12.15 closing price of £3.80)	Requirement met Yes/No
Jayne-Anne Gadhia	£725,000	200%	381,579	1175%	£8,520,554	Yes
Former Directors who served in 2015 (shareholding at date stepped down from Board)						
Lee Rochford	£475,000	150%	187,500	166%	£789,818	Yes

1 In respect of Mr Rochford, the current shareholding reflects the number of shares held at the date he stepped down from the Board. The shareholder guidelines for 2015 set out that the Chief Financial Officer was expected to hold 150% of salary in shares of Virgin Money.

Directors' Remuneration Report

Breakdown of share interests

The share numbers referred to in this section are adjusted for the effect of the re-organisation of the Company share capital on listing in 2014.

IPO Incentive Scheme

Awards were granted under the IPO Incentive Scheme on 19 December 2013, and designed to focus participants on a successful listing of the Company by December 2016. The total value of the award was confirmed on listing by reference to the IPO value and the corresponding total number of Ordinary Shares was 333,215 for the Chief Executive and 222,143 for the former Chief Financial Officer. To date, 80% of the award has vested (40% on listing and 20% in December 2014, 20% December 2015); the remaining 20% vests in December 2016. Holding periods of six months apply to each deferred tranche. All awards are subject to malus and clawback provisions.

	At 1 Jan 2015	Awarded during the year	Vested during the year	Lapsed during the year	Unvested as at 31 Dec 2015	Date of grant	Market value at grant[1]	Notes
Jayne-Anne Gadhia	133,286	–	66,643	–	66,643	19 December 2013	n/a	
Former Directors who served in 2015								
Lee Rochford	88,858	–	44,428	–	44,430	19 December 2013	n/a	

1 The Company was in private ownership at the date of grant and therefore no market value was available at that time.

FY12 and FY13 Phantom Share Awards

Awards were granted prior to IPO under a deferred bonus plan known as the 'Phantom Incentive Plan'. These awards were valued by reference to the Tangible Net Asset Value (TNAV) of the Company. On listing, all phantom share awards converted into an equivalent award over Ordinary Shares. No further phantom share awards have been granted since listing. No further performance conditions apply, although the awards remain subject to the malus and clawback policy described on page 120. Holding periods of six months apply to each deferred tranche.

	At 1 Jan 2015	Awarded during the year	Vested during the year	Lapsed during the year	Unvested as at 31 Dec 2015	Date of grant	Market value at grant[1]	Notes
Jayne-Anne Gadhia	485,160	–	–		485,160	18 July 2013	n/a	FY2012 deferred bonus
	203,420	–	–		203,420	27 February 2014	n/a	FY2013 deferred bonus
Former Directors who served in 2015								
Lee Rochford	113,540	–	–		113,540	27 February 2014	n/a	FY2013 deferred bonus

1 The Company was in private ownership at the date of grant and therefore no market value was available at that time.

Recruitment Award

An individual share based recruitment award was made to the former Chief Financial Officer in 2013 to compensate for forfeited awards from previous employment.

	At 1 Jan 2015	Awarded during the year	Vested during the year	Lapsed during the year	Unvested as at 31 Dec 2015	Date of grant	Market value at grant	Notes
Former Directors who served in 2015								
Lee Rochford	209,620	–	106,720	–	102,900	23 December 2013	n/a	

FY14 DBSP

Awards were granted under the Deferred Bonus Share Plan on 26 March 2015 in respect of deferred bonus awards for FY14 performance. The face value of the award was 152% of fixed pay for the Chief Executive and 150.4% of salary for the former Chief Financial Officer. These were converted into the number of shares shown using the share price on the day immediately preceding grant. 25% of the award vested at grant; 37.5% is scheduled to vest in March 2018 and 37.5% is scheduled to vest in March 2019. No further performance conditions apply, although the awards remain subject to the malus and clawback policy described on page 120. Holding periods of six months apply to each deferred tranche.

	At 1 Jan 2015	Awarded during the year	Vested during the year	Lapsed during the year	Unvested as at 31 Dec 2015	Date of grant	Market value at grant[1]	Notes
Jayne-Anne Gadhia	–	295,427	73,857	–	221,570	26 March 2015	409p per share	
Former Directors who served in 2015								
Lee Rochford	–	166,552	41,638	73,300	51,614	26 March 2015	409p per share	

1 Awards are made based on the market value of ordinary shares determined on the dealing day preceding the date of grant. The market value reported represents the share price on 25 March 2015.

FY15 LTIP

Awards were granted under the Long Term Incentive Plan on 26 March 2015. The face value of the award was 120% of fixed pay for the Chief Executive and 120% of salary for the former Chief Financial Officer. These were converted into the number of shares shown using the share price on the day immediately preceding grant. One third of the award is scheduled to vest on 26 March 2018, one third of the award is scheduled to vest on 26 March 2019. The final third of the award is scheduled to vest on 26 March 2020. Awards are subject to performance conditions (as described in last year's report). Holding periods of six months apply to each deferred tranche. All awards are subject to malus and clawback provisions.

	At 1 Jan 2015	Awarded during the year	Vested during the year	Lapsed during the year	Unvested as at 31 Dec 2015	Date of grant	Market value at grant[1]	Notes
Jayne-Anne Gadhia	–	278,875	–	–	278,875	26 March 2015	409p per share	
Former Directors who served in 2015								
Lee Rochford	–	139,364	–	87,270	52,094	26 March 2015	409p per share	

1 Awards are made based on the market value of ordinary shares determined on the dealing day preceding the date of grant. The market value reported represents the share price on 25 March 2015.

Directors' Remuneration Report

Former Chairman's interest in share options

The options were awarded in order to secure the former Chairman's appointment in October 2011 and are fully vested and exercisable. The options will lapse ten years after the date of Admission (18 November 2014). The number of Ordinary Shares subject to the options will be increased in accordance with the terms of the option agreement in the event of the exercise of certain warrants over Ordinary Shares in the Company.

	At 1 Jan 2015	Granted during the year	Exercised during the year	Lapsed during the year	Not exercised as at 31 Dec 2015	Exercise price	Exercise period
Sir David Clementi	625,328	–	–	–	625,328	£2.15	To 18 November 2024

Additional disclosures

Directors' interest – summary of awards vested and purchases and sales made by directors in 2015

	Holding at 1 January 2015 (or appointment date)	Transactions during year	Number of shares	Notes	Holding at 31 December 2015 (or date stepped down from Board)
Jayne-Anne Gadhia	**2,168,847**	26 March 2015	38,194	Net number of shares from vesting of first tranche of FY14 DBSP	**2,242,251**
		19 December 2015	35,210	Net number of shares from vesting of third tranche of IPO Incentive	
Colin Keogh	**137,260**	–	–	–	**137,260**
Norman McLuskie	**90,080**	–	–	–	**90,080**
Marilyn Spearing	**–**	–	–	–	**–**
Patrick McCall	**–**	–	–	–	**–**
Gordon McCallum	**–**	18 September 2015	18,983	Purchase of shares	**18,983**
Glen Moreno	**–**	8 December 2015	25,000	Purchase of shares	**25,000**
Geeta Gopalan	**–**	–	–	–	**–**
Former Directors who served in 2015					
Lee Rochford	**129,907**	26 March 2015	21,532	Net number of shares from vesting of first tranche of FY14 DBSP	**207,847**
		31 March 2015	56,408	Net number of shares from vesting of second tranche of recruitment award	
Olivia Dickson	**–**	–	–	–	**–**
James Lockhart III	**–**	–	–	–	**–**
Sir David Clementi	**–**	–	–	–	**–**

Directors' Report

Corporate governance report

The Corporate Governance Report can be found on pages 81 to 110 and, together with this report of which it forms part, fulfils the requirements of the Corporate Governance Statement for the purpose of the Disclosure and Transparency Rules (DTR).

Results

The consolidated income statement shows a statutory profit before tax for the year ended 31 December 2015 of £138.0 million.

Dividends

On 28 July 2015, the Board announced that it had declared and approved an interim dividend of 1.4 pence per Ordinary Share which was paid on 9 October 2015 to shareholders on the register at the close of business on 28 August 2015.

On 1 March 2016, the Board recommended a final dividend of 3.1 pence per Ordinary Share in respect of the full financial year ended 31 December 2015 which will, subject to approval by shareholders at the 2016 Annual General Meeting (AGM), be payable on 25 May 2016. Further information on dividends is shown in note 11 of the financial statements and is incorporated into this report by reference.

Post balance sheet events

On 25 January 2016, the Group raised £803.0 million from institutional investors through the issuance of Residential Mortgage Backed Securities in the Gosforth Funding 2016-1 transaction.

Going concern

The going concern of the Company and the Group is dependent on successfully funding the balance sheet and maintaining adequate levels of capital. In order to satisfy themselves that the Company and the Group has adequate resources to continue to operate for a period of at least 12 months from the date of approval of this report, the Directors have considered a number of key dependencies which are set out in the Risk Overview and Risk Management Report sections under Principal Risks on pages 50 to 53, Funding and Liquidity on pages 191 to 201 and Capital Position on pages 202 to 208 and additionally have considered projections for the Company and the Group's capital and funding position.

Having considered these and made appropriate enquiries, the Directors consider that the Company and Group have adequate resources to continue in business for a period of at least twelve months from the date of approval of this report. As a result, it is appropriate to continue to adopt the going concern basis in preparing the accounts.

Viability statement

The viability statement is contained in the Risk Overview Section on pages 52 to 53 and is incorporated into this report by reference.

Directors

The names and biographical details of the current Directors are shown on pages 74 to 77. Particulars of their emoluments and interests in shares in the Company are given on pages 125 to 134 of the Directors' Remuneration Report.

Changes to the composition of the Board since 1 January 2015, and up to the date of this report, are shown in the table below. Further details of Board changes can be found on page 88 of the Corporate Governance Report.

Name	Role	Date of appointment	Date of retirement
Glen Moreno	Chairman	1 January 2015[1]	
Geeta Gopalan	Independent Non-Executive Director	25 June 2015	
Sir David Clementi	Chairman		30 June 2015[2]
Lee Rochford	Chief Financial Officer		31 August 2015
James Lockhart III	Non-Executive Director		11 September 2015
Olivia Dickson	Independent Non-Executive Director		31 December 2015

1. Became Chairman on 21 May 2015.

2. Retired as Chairman on 21 May 2015.

Directors' Report

Appointment and retirement of Directors

The appointment, retirement and/or replacement of Directors is governed by the Articles of Association of the Company (Articles), the 2014 Edition of the UK Corporate Governance Code (Code) and the Companies Act 2006 (Act). The Articles may only be amended by a special resolution of the shareholders in a general meeting.

Geeta Gopalan has been appointed to the Board since the 2015 AGM and will therefore stand for election by shareholders for the first time at the forthcoming AGM. In the interests of good governance, all of the other Directors will also retire and those wishing to serve again will submit themselves for re-election at the 2016 AGM.

Directors' indemnities

The Directors, including former Directors who stepped down during the year, have entered into individual deeds of indemnity with the Group which constitute "qualifying third party indemnity provisions" for the purposes of the Act. The deeds indemnify the Directors to the maximum extent permitted by law and remain in force for the duration of a Director's period of office and for a six year period thereafter. The deeds were in force during the whole of the financial year or from the date of appointment for those Directors appointed in 2015. Deeds for existing Directors are available for inspection at the Company's registered office. In addition, the Group had appropriate Directors' and Officers' insurance cover in place throughout 2015.

Financial risk management objectives and policies

The Group provides a wide range of banking and financial services through a range of channels, including online and mobile, intermediaries, call centres and a national network of 75 stores and six customer Lounges.

Information about internal controls and financial risk management systems in relation to financial reporting and Board review thereof can be found on page 101 of the Audit Committee Report.

Information about financial risk management objectives and policies in relation to the use of financial instruments can be found in the Risk Management Report beginning on page 139.

Both sections of the annual report are incorporated into this report by reference.

Information included in the Strategic Report

The following information that would otherwise be required to be disclosed in this report and which is incorporated into this report by reference can be found on the following pages of the Strategic Report:

Subject matter	Page reference
Future developments	24 to 28
Employment of disabled persons	33
Colleague engagement	33
Emissions reporting	43

Disclosure of information under Listing Rule (LR) 9.8.4R

Additional information required to be disclosed by LR9.8.4, where applicable to the Group, can be found in the following sections of this report:

Subject matter	Page reference
Relationship agreements	93 to 94
Emolument waivers	130
Publication of unaudited financial information	140 and Note 36, pages 267 to 268
Dividend waivers	Note 11, page 246
Allotment of equity securities	Note 29, page 258
Significant contracts	Note 37, page 269

Share capital, control and Directors' powers

Information about share capital, restrictions on the transfer of shares or voting rights, and special rights with regard to control of the Company is shown in note 29 to the financial statements and is incorporated into this report by reference.

The Company operates an employee benefit trust (EBT), which holds Ordinary Shares on trust for the benefit of employees and former employees of the Group, and their dependents, and which is used in conjunction with the Group's employee share schemes. Whilst Ordinary Shares are held in the EBT, the voting rights in respect of these Ordinary Shares can be exercised by the trustees of the EBT.

The powers of the Directors, including in relation to the issue or buy back of the Company's shares, are set out in the Act and in the Articles. The Directors were granted authorities to issue and allot shares and to buy back shares at the 2015 AGM.

Shareholders will be asked to renew these authorities in line with the latest institutional shareholder guidelines at the 2016 AGM.

The Company did not repurchase any of the issued Ordinary Shares during the year, up to the date of this report or in 2014. During 2014 all Deferred Shares were repurchased from shareholders immediately prior to listing on the London Stock Exchange.

Substantial shareholders

Information provided to the Company by substantial shareholders pursuant to the DTR is published via a Regulatory Information Service. As at 31 December 2015, the Company has been notified under DTR Rule 5 of the interests as set out below in its issued share capital. All such share capital has the right to vote in all circumstances at general meetings.

In the period from 31 December 2015 to the date of this report, the Company has received notifications from BlackRock, Inc. As at the date of this report, those notifications indicate that BlackRock, Inc's shareholding is 22,617,824 Ordinary Shares representing 5.09% of the total voting rights attaching to issued share capital.

During the course of the year, the Company's "controlling shareholder" (for the purposes of the Listing Rules), Virgin Financial Investments Limited, transferred its entire shareholding to Virgin Group Holdings Limited.

As at 31 December 2015 Shareholder	Ordinary shares held	% of voting rights	Direct/ indirect interest
Virgin Group Holdings Limited	155,120,454	34.96	Direct
WLR IV VM LLC and WLR IV VM II LLC	52,996,220	12.00	Direct
FMR LLC	34,253,209	7.71	Indirect
BlackRock, Inc	22,242,848	5.01	Indirect
Kames Capital plc	14,388,450	3.25	Indirect/Direct
York Capital Management Global Advisors LLC	14,297,618	3.23	Indirect

Change of control

The Company is not a party to any significant contracts that are subject to change of control provisions in the event of a takeover bid, other than the Virgin Money Trademark Licence Agreement. This is the agreement under which Virgin Enterprises Limited (VEL) grants a perpetual licence to Virgin Money providing the right to use the "Virgin" and "Virgin Money" trademarks. VEL has the right to terminate the agreement in the event of a change of control, other than a change of control pre-approved by VEL. VEL shall only be entitled to withhold consent in the event of a takeover by a third party who, in VEL's reasonable opinion, is a direct competitor of VEL or any Virgin entity in the UK, or whose reputation or financial standing is reasonably likely to damage materially the value or reputation of the "Virgin" brand.

There are no agreements between Virgin Money and its Directors or employees which provide compensation for loss of office or loss of employment that occurs because of a takeover bid.

In the event of a takeover or other change of control (excluding an internal reorganisation), outstanding awards under the Group's share plans vest to the extent any applicable performance conditions have been met, and subject to applicable time pro-rating, in accordance with the rules of the plans.

Research and development activities

Virgin Money does not undertake formal research and development activities although it does invest in the development of platforms and products.

Statement of directors' responsibilities

The Directors are responsible for preparing the annual report and the Group and parent company financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare Group and parent company financial statements for each financial

Directors' Report

year. Under that law, they are required to prepare the Group financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and applicable law and have elected to prepare the parent company financial statements on the same basis.

Under company law, the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and parent company, and of the profit or loss for that period. In preparing each of the Group and parent company financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRS as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the parent company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent company's transactions and disclose with reasonable accuracy, at any time, the financial position of the parent company and enable them to ensure that its financial statements comply with the Act. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the Directors are also responsible for preparing a Strategic Report, Directors' Report, Directors' Remuneration Report and Corporate Governance Statement that comply with that law and those regulations.

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

Responsibility statement of the Directors in respect of the Annual Financial Report

Each of the current Directors, who is in office at the date of this report and whose name is listed on pages 74 to 77, confirms that to the best of his or her knowledge:

- the financial statements, prepared in accordance with the applicable set of accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company and the undertakings included in the consolidation taken as a whole; and
- the Strategic Report and Directors' Report include a fair review of the development and performance of the business and the position of the Company and Group together with a description of the principal risks and uncertainties that they face.

The Directors consider that the annual report and accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Group's position and performance, business model and strategy.

Independent auditor and audit information

Each of the current Directors, who is in office at the date of this report and whose name is listed on pages 74 to 77, confirms that, so far as the Director is aware, there is no relevant audit information of which the Company's auditor, KPMG LLP, is unaware and that he or she has taken all the steps that he or she ought to have taken as a Director to make himself or herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information. This confirmation is given and should be interpreted in accordance with the provisions of the Act.

Resolutions concerning the appointment of a new auditor, PricewaterhouseCoopers LLP (PwC), and authorising the Audit Committee to set PwC's remuneration will be proposed at the 2016 AGM. PwC is recommended for appointment following the competitive tender process described on page 102.

On behalf of the Board:

KJ Marshall

Katie Marshall
1 March 2016
Company Secretary

Virgin Money Holdings (UK) plc
Registered No. 03087587

Risk Management Report

Virgin Money London Marathon

Risk Management Report

The Group's Approach to Risk

Risk management is at the heart of the Group's strategy to deliver sustainable growth, quality and returns. This is achieved through a prudent risk appetite and informed risk decision making, supported by a consistent risk-focused culture across the Group.

This risk management section provides additional information on how risk is managed within the Group. It details the Group's risk culture, appetite for risk, the approach to risk governance, committee structures, stress testing and a full analysis of risk classes – the framework used to identify, manage, mitigate and monitor risk.

Each risk class is described using the following headings: definition, risk appetite, exposures, measurement, mitigation and monitoring.

The Group takes a prudent approach to risk with rigorous management controls to keep the Group safe. The Group has a strong and independent Risk Function with a duty to maintain a robust risk management framework, identify and escalate emerging risks and support sustainable business growth within risk appetite achieving an appropriate balance of risk and reward.

Risk culture

The Group articulates its risk values which describe how it expects all colleagues, suppliers and partners to operate. They are outlined below:

- **Do the right thing** – "Don't just do things right..."
- **Challenge the status quo** – "Don't sit back and say nothing..."
- **Understand your responsibilities** – "Be personally accountable for your actions and decisions..."

The Board ensures that senior management implements risk appetite and policies that either limit or, where appropriate, prohibit activities that could be detrimental to the Group.

The Group has a customer focused, low risk business model built on a prudent risk culture. The focus remains on building and sustaining long-term relationships with customers whatever the economic climate.

Risk appetite

- the Group defines risk appetite as the amount and type of risk that the Group is prepared to seek, accept or tolerate;
- strategy is developed in conjunction with risk appetite. A Risk Appetite Statement is approved by the Board with each strategic planning cycle. This incorporates recommendations from Non-Executive Directors;
- risk appetite is embedded within principles, policies, authorities and limits; and
- risk appetite evolves and reflects external market developments and the development of the Group.

All disclosures in the Risk Management Report are unaudited, unless otherwise stated. Additional disclosures can be found in the Pillar 3 disclosures, found on the Group's website.

The Group's Approach to Risk

Balance Sheet Strength		
Capital	**Liquidity**	**Profitability**
The Group maintains a high-quality capital base, targeting capital ratios which support business development and the risks inherent in the strategic plan and in excess of regulatory requirements.	The Group operates an investment strategy for treasury assets which prioritises liquidity and ensures that the Group holds a liquid asset buffer in excess of internal analysis and regulatory guidance.	Achieving appropriate profitability across all business lines is essential to the sustainability of Virgin Money.
Depositor protection	**Minimise unrewarded risks**	**Mature control environment**
As an authorised deposit taker, the Group ensures that depositors' financial assets and all customers' personal data are protected.	Unrewarded risks only expose the Group to downside risk. The Group avoids unrewarded risks where possible or controls them as far as is economically feasible.	The Group ensures that the control environment is fit for purpose, supporting the business as it grows in terms of people, processes and systems.

Governance and control

- a strong governance framework remains a priority for the Group. It is the foundation for the delivery of effective risk management;
- governance is maintained through delegation of authority from the Board to executive management and committees, and is designed to promote open challenge. The Group's risk appetite, policies, procedures, controls and reporting are in line with regulations, law, corporate governance and industry good-practice;
- Board-level engagement, coupled with the direct involvement of senior management in risk issues at the Executive Committee, ensures that issues are promptly escalated and remediation plans are initiated where required;
- the approach to risk is founded on a robust risk management framework and a strong control culture which ensures accountability for risk and guides the way all colleagues operate; and
- the interaction of the executive and non-executives is transparent and open, an approach encouraged by both the Board and senior management.

Risk decision-making and reporting

- taking risks which are well understood, consistent with strategy and have appropriate returns is a key driver of sustainable shareholder value;
- risk analysis and reporting supports the identification of opportunities and risks;
- a current and forecast view of the Group's overall risk profile, key exposures and management actions, and performance against risk appetite is reported to and discussed monthly at the Risk Management Committee. The Risk Management Committee reports to the Board Risk Committee and the Board;
- rigorous stress testing exercises are carried out to assess the impact of a range of adverse scenarios with different probabilities and severities to inform strategic planning; and
- the Chief Risk Officer regularly informs the Board Risk Committee and the Board of the risk profile and has direct access to the Chairman.

Risk Management Report

The Group's Approach to Risk

Exposure to risk arising from the business activities of the Group

The table below provides a high-level guide to how the Group's business activities are reflected in risk-weighted assets.

Virgin Money Group

Total risk-weighted assets £6,110m

Mortgages and savings

Residential mortgages
Buy-to-let mortgages
Customer deposits

Risk-weighted assets	£m
Credit risk	3,953
Operational risk	331
Market risk[1]	0

Credit cards

Credit cards

Risk-weighted assets	£m
Credit risk	1,193
Operational risk	142
Market risk[1]	0

Current accounts Insurance and Investments

Current accounts
Pensions
Insurance
Investments

Risk-weighted assets[2]	£m
Credit risk	0
Operational risk	52
Market risk[1]	0

Central functions

Shared support functions
Interest Rate Risk in the Banking Book[3]

Risk-weighted assets	£m
Credit risk	425
Operational risk	0
Market risk[1]	0
CVA	14

1 Virgin Money does not have a trading book.

2 The capital requirements for Virgin Money Unit Trust Managers Limited and Virgin Money Personal Financial Service Limited have been met, with a Common Equity Tier 1 ratio of 94% and 96%, respectively.

3 Only Pillar 2 capital is held for Interest Rate Risk in the Banking Book. There is no associated risk-weighted asset measure.

Principal risks

The Group's principal risks are shown in the Risk Overview (pages 50 to 53). The Group's emerging risks are shown on pages 143 and 144. Full analysis of the Group's risk classes is on pages 152 to 208.

Emerging Risks

The Group considers the following to be risks that have the potential to increase in significance and affect the performance of the Group.

Macroeconomic environment

While confidence is increasing in the stability of the UK financial system, there is a risk of contagion from increasing market volatility and geo-political uncertainty in other regions, leading to a slow down in economic growth and a delay to expected increases in base rate. A lower for longer interest rate puts pressure on net interest margins and therefore business and financial performance. The potential for the UK to exit the European Union in the upcoming referendum could result in disruption to the UK consumer, UK economy and Europe more broadly.

Key mitigating actions

- the Group regularly reviews earnings in light of economic forecasts. The Group continues to test its readiness to respond to future increases in base rate and regularly assesses financial and operational impacts and customer implications such as affordability and vulnerability;
- the Group continues to ensure there is an appropriate balance between profitability and customer outcomes using the EBO approach and philosophy; and
- the Group monitors customer behaviours, liquidity position, counterparty vulnerability, operational capability and disruption to payment and other systems in its Brexit contingency planning.

Buy-to-let lending

In December 2015, the BoE Financial Stability Report cited concerns over the growth in buy-to-let (BTL) lending and the impact that a structural shift to the private rental sector may have on market stability. In addition, there have been several tax and regulatory changes that may collectively weaken the attractiveness of BTL to an investor. These changes have added uncertainty to the outlook of BTL for both landlords and lenders, particularly over the medium to long-term.

Key mitigating action

- the Group is monitoring developments in this sector closely and will make the required amendments to lending policy, where appropriate.

Cybercrime

Cyber attack is a serious and growing threat to the resilience of the UK financial system, reflecting increased use of technology in financial services. Resilience to cyber attack and the ability to recover quickly from attacks that inevitably occur are priorities in a cybercrime landscape and threat environment that continues to evolve. This is in the context of digital technology that is changing customer behaviour, leading to changes in banking models.

Key mitigating actions

- the Group has increased the focus on digital capability and IT resilience; and
- the Group continues to invest in enhancing information security, fraud and anti-money laundering capability considering both the external threat environment and the changing risk profile of the business.

Regulatory capital requirements

While there is now greater clarity on regulatory capital requirements, there remains some uncertainty as the UK and European regulatory frameworks continue to evolve. The Basel III global regulatory standards on bank capital adequacy, stress testing and market and liquidity risk management aim to strengthen regulation, supervision and risk management in the banking sector. The Group is compliant with current CRD IV / CRR requirements and will continue to respond to new guidance and technical standards as they are published.

Key mitigating actions

- the Board is focused on responding effectively, and in a timely manner, to changes in the regulatory environment;
- the business planning process incorporates the Group's forward view of emerging capital requirements;
- regulatory horizon scanning ensures that risks are mitigated within the context of risk appetite;
- the Group continues to invest in and develop up to date risk management frameworks, systems and processes; and
- the Group undertakes stress and scenario testing as an integral part of its strategic and capital planning.

Risk Management Report

Emerging Risks

Competition regulation

Regulatory and competition authorities continue to review key banking markets. Market inefficiencies and consolidation within the sector could change the competitive landscape and possibly impact market structures and margins.

Key mitigating actions

- the Group is an active participant in the broad range of regulatory developments, including the Competition and Markets Authority investigation into current account and business banking sectors; and
- the Group is supporting the FCA market studies into credit card and cash savings, and will actively participate in the consultation process on proposed remedies.

Banking Reform

The Financial Services (Banking Reform) Act 2013 introduces a ring-fence for UK retail banks, with the aim of separating core banking services critical to individuals and small and medium-sized enterprises from wholesale and investment banking services. The Group anticipates being a fully ring-fenced bank by the 2019 implementation date and is preparing for this change. The Group has responded to changes to the PRA's rules implementing the EU Bank Recovery and Resolution Directive.

Key mitigating actions

- the Group has ongoing engagement with HM Treasury, the PRA and the BoE on the evolving UK regulatory framework and the impact of EU directives; and
- resources have been mobilised to assess the impacts of ring-fencing and propose potential responses to consultation which are aligned to the Group's strategy.

Supplier partnerships

The Group manages outsourced relationships with parties who support the credit card, investment and insurance business lines. The Group have strategic suppliers for key components of its infrastructure. Reliance on key corporate partners and strategic suppliers involves the potential risk of disruption to service arising from the failure of a third party.

Key mitigating actions

- the Group continues to develop its supplier partnership and oversight capability to minimise the risk of service disruption caused by the failure of a third party; and
- the Group engages specialist third parties to undertake targeted reviews of supplier performance as required.

Unit trust management

Virgin Money Unit Trust Managers Limited (VMUTM) is exposed to movements in stock markets. The sole income stream of VMUTM is reliant upon investment fund performance.

Key mitigating action

- the Group currently mitigates the risk associated with stock market movements and their impact on earnings through the use of a FTSE hedge.

Risk Governance

The Group's risk management framework provides a strong and consistent approach to risk management and drives a risk profile in line with risk appetite. It articulates accountabilities for risk management and control, oversight and assurance. It supports the discharge of responsibilities to customers, shareholders and regulators and establishes a common risk language. The risk management framework assigns the risks the Group is exposed to into classes which are used consistently to support risk reporting.

The risk governance structure below is integral to implementing the risk management framework by ensuring Risk has appropriate representation on key committees. This ensures relevant discussion of the risk profile and outlines the flow and escalation of risk information and reporting from functional Risk Boards to the Executive Committees and the Board. Strategic direction and guidance is cascaded down from the Board and the Executive Committees.

Board

Chairman: Glen Moreno

Board Committees[1]

Risk Committee	Audit Committee	Remuneration Committee
Chairman: Colin Keogh (Non-Executive Director)	**Chairman: Norman McLuskie (Non-Executive Director)**	**Chairman: Marilyn Spearing (Non-Executive Director)**

Executive Committees

Risk Management Committee	Asset and Liability Committee
Chairman: Chief Risk Officer	**Chairman: Chief Financial Officer**
Identifies and recommends risk appetite, manages risk within agreed limits, monitors key risk exposures in relation to risk strategy and recommends the approach to managing all types of risk.	Responsible for management and monitoring of liquidity, funding, capital and asset and liability management within agreed risk appetite and policy.

Management Committees

Operational Risk, Conduct Risk and Compliance Committee	Credit Risk Committee	Treasury Risk Committee

Functional Risk Boards

1 Additional Board Committee comprises of a Nomination Committee.

Risk Management Report

Risk Management

Role of the Board and senior management

The key responsibilities of the Board and senior management include:

- setting risk appetite and agreeing the risk management framework;
- approving risk policies, supporting development of appropriate risk management practices;
- cascading delegated authority (e.g. to Board committees and the Chief Executive); and
- effectively overseeing risk management, consistent with risk appetite.

Committees

The Board and Executive Committee structure is designed to oversee the overall management of risk, aligned with strategy and risk appetite. The structure is based on a current and comprehensive risk profile that identifies all material risks to the Group. The governance structure is underpinned by well understood policies that are accessible and comply with regulations.

Three Lines of Defence model

The Group uses a 'Three Lines of Defence' model which defines clear responsibilities and accountabilities and ensures effective independent assurance activities take place covering key decisions.

- line management (first line) have primary responsibility for risk decisions, measuring, monitoring and controlling risks within their areas of accountability. They are required to establish effective controls in line with policy, to maintain appropriate risk management skills, practices and tools, and to act within risk appetite parameters set and approved by the Board.
- Risk (second line) is a centralised function providing proactive advice and constructive challenge to the effectiveness of risk decisions taken by management. It has a key role in promoting the implementation of a strategic approach to risk management reflecting the risk appetite and risk management framework agreed by the Board. This encompasses:
  - embedded and effective risk management processes;
  - transparent and focused risk monitoring and reporting;
  - expert high-quality advice and guidance to the Board, executives and management on strategic issues and horizon scanning for upcoming regulatory changes;
  - reviewing, challenging and reporting on the risk profile of the Group, ensuring mitigating actions are appropriate;
  - providing assurance to meet internal and external obligations;
  - promoting a constructive working environment in which the Risk Function is trusted and respected; and
  - effective dialogue with the first line through advice, development of common methodologies, education, training and development of new tools.

Risk Management

- Internal Audit (third line) provides independent, objective assurance to add value and improve operations. It helps the Group achieve its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

Risk management in the business

The Group identifies and manages risks inherent in the business through the activities of management. This ensures that business decisions strike an appropriate balance between risk and reward, consistent with the Group's risk appetite.

All functional areas complete a monthly risk and control attestation and a quarterly control effectiveness review.

This allows the Group to ensure controls are fit for purpose or, if required, implement remedial action. Executives from each business area and Executive Committee members challenge and certify the appropriateness of these functional assessments.

Control effectiveness reviews are an important mechanism for developing and embedding risk policies and management strategies aligned with the risks faced by the business.

Role of the Risk Function

The Risk Function has four specialist teams and is headed by the Chief Risk Officer. These teams provide oversight and independent challenge to line management and support senior management and the Board with independent reporting on risks and opportunities. Risk Directors, responsible for specific risk classes, meet on a regular basis with the Chief Risk Officer to review and assess the risk profile of the Group and to ensure that mitigating actions are appropriate.

The Chief Risk Officer is accountable for developing and leading a Risk Function that adds value to the Group by:

- proposing risk appetite to the Board for approval, and reporting the performance of the Group against approved risk appetite;
- developing an effective and compliant risk management framework for approval by the Board, and overseeing its execution and compliance;
- providing a regular comprehensive view of the Group's risk profile, key risks (both current and emerging), and management actions;
- challenging the Executive on emerging risks and providing expert risk and control advice to help maintain an effective risk management framework; and
- maintaining a good working relationship with key regulators.

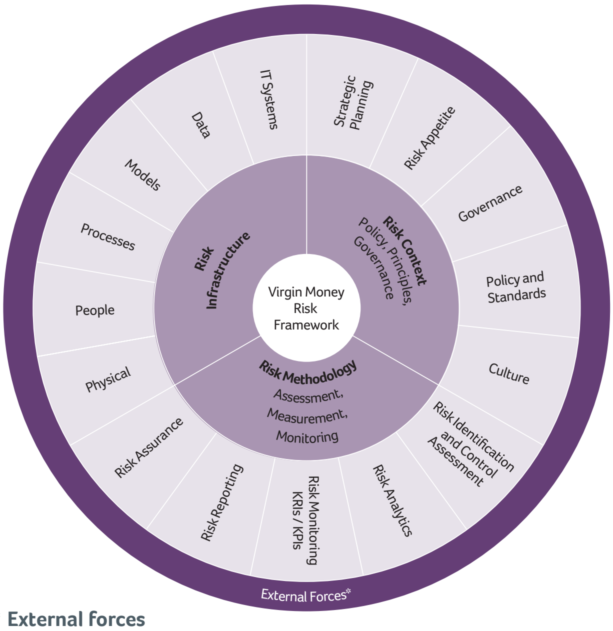
Risk Directors leading the four specialist teams:

- provide independent advice, oversight and challenge to the business;
- develop and maintain policies, specific risk frameworks and guidance to align business initiatives with regulatory requirements; and
- establish and maintain appropriate governance structures, culture, oversight and monitoring arrangements which ensure robust and efficient compliance with relevant risk appetite and policies.

Risk Management Report

Risk Management framework

The risk management framework is structured around the components below:



* **External forces**
Legal
Regulatory
Economic
Customer
Competitor
Supplier/Partner
Political
Technological

Culture

The risk management framework is supported by the underlying culture and values of the Group. To manage risk effectively across the organisation, management have a clear understanding of risk appetite, business strategy, expected behaviour and a commitment to the role they play.

A number of levers are used to reinforce the risk culture including tone from the top, governance, clear accountabilities, effective communication and challenge, and appropriately aligned performance management and reward.

Risk identification and control assessment

The process to identify, measure and control risk is integrated into the overall framework for risk governance. Risk identification processes are forward-looking to ensure emerging risks are identified. Risks are captured in comprehensive risk logs and measured using robust and consistent methodologies. Measurement of risks include the application of sound stress testing and scenario analysis, and considers whether relevant controls are in place before exposures are taken.

Risk analytics, monitoring and risk reporting

Risks are logged and reported on a monthly basis, or as frequently as necessary, to the appropriate governance committee. The quantum of the risk is compared to the overall risk appetite and specific limits or triggers. When limits or triggers are breached, committee minutes are clear on the actions and timeframes required to resolve the breach and bring risk within tolerance.

Resources and capabilities

Appropriate mechanisms are in place to avoid over-reliance on key personnel or systems/technical expertise. Adequate resources are available to deal with customers both under normal working conditions and in times of stress. Flexible practices ensure that the level of available resource can be increased if required. Colleagues undertake appropriate training to ensure they have the skills and knowledge necessary to enable them to deliver fair outcomes for customers, being mindful of the requirements of policies, the FCA and the PRA.

Independent challenge

Internal Audit provides independent assurance to the Audit Committee and the Board that risks within the Group are recognised, monitored and managed within acceptable parameters. Internal Audit is fully independent of the Risk Function, and seeks to ensure objective challenge to the effectiveness of the risk management framework.

Risk Classes

The Group's risk framework covers all types of risk which affect the Group and could impact on the achievement of strategic objectives. A detailed description of each category is provided on pages 152 to 208.

- **Credit Risk Page 152**
  - Retail
    - Mortgage
    - Personal Current Accounts
    - Credit Cards
    - Collections & Recoveries
    - Responsible Lending
  - Wholesale
    - Wholesale Credit Risk
    - Large Exposures
- **Market Risk Page 177**
  - Foreign Exchange Risk
- **Operational Risk Page 182**
  - Operational Risk Framework
  - Corporate Risks
  - Operational Risk Losses
- **Other Operational Risk Page 182**
  - Fund Management
  - Legal Risk
  - Business Disruption
  - Information Security
  - Information Management
  - Financial Crime
  - People
  - Process
  - Systems
  - Payment & Settlement Risk
  - Physical Security & Safe Environment
  - Non-financial Counterparty Risk
- **Conduct Risk and Compliance Page 184**
  - Conduct
    - Product Design and Governance
    - Unfair Contract Terms
    - Sales Practices, Advice & Culture
    - Sales Incentives and Reward
    - Quality and Competence
    - Post sale Administration & Transaction Handling
    - Partner Conduct
    - Vulnerable Customers & Treating Customers Fairly
  - Compliance
    - Upstream Regulation
    - Regulatory Reporting
    - Critical and Important Outsourcing
    - Senior Persons Regime
    - Privacy and Data Protection
    - Sourcebooks CASS COLL MCOB BCOB BIPRU COB CCA REMCODE
    - Markets Compliance
- **Strategic and Business Risk Page 45**
  - Macro-economic Risk
  - Transformation Risk
  - Change Risk Management
  - Reputation Risk Management
  - Competitive Environment
- **Financial Risk Page 186**
  - Interest Rate Risk in the Banking Book
  - Retail Concentration Risk
  - Secured Wholesale Debt
  - Pricing
  - Model Risk
  - Wholesale Credit Concentration Risk
  - Under-estimation of Credit Risk
- **Liquidity Page 191**
  - Retail Funding Risk
  - Off-Balance Sheet Liquidity Risk
  - Marketable Asset Risk
  - Non-Marketable Asset Risk
  - Franchise Viability Risk
  - Wholesale Funding Risk
  - Funding Concentration Risk
  - Intra-Day Liquidity Risk
- **Capital Page 202**
  - Capital Sufficiency
  - Capital Efficiency

Risk Management Report

Stress Testing

Stress testing is recognised as an essential risk management tool within the Group.

Stress testing is undertaken to further understand the vulnerabilities that the business model faces under adverse conditions and potential extent of current or future exposures.

Stress testing is embedded in the planning process and is applied to the base case business plan. This allows senior management and the Board to assess the base case plan in adverse circumstances and to adjust strategies accordingly. This also facilitates the development of mitigating actions if the plan does not meet risk appetite in a particular stressed scenario. A rigorous review and challenge process ensures that senior management are involved in the design of stress tests and in responding to the results.

The Group uses scenario stress testing to:

- assess the base case business plan against risk appetite, alongside a comparison of the plan in adverse circumstances, to ensure the Group remains within risk appetite;
- develop mitigating actions and contingency plans to address potential impacts of adverse scenarios. Stress testing outputs also link directly to the recovery planning process;
- support the Internal Capital Adequacy Assessment process (ICAAP), the Individual Liquidity Adequacy Assessment (ILAA) and inform the setting of regulatory guidance; and
- meet the standards required and information needs of internal and external stakeholders, including regulators.

On an annual basis, or more frequently if required, the Group conducts a macroeconomic stress testing exercise based on the strategic business plan. The exercise aims to highlight the key vulnerabilities of the Group to adverse changes in the economic environment and ensures that there are adequate financial resources in the event of a downturn. The exercise includes the PRA UK Variant Stress Scenario (these are the PRA's published supervisory recommended scenarios for the UK, details of which are publicly available on the Bank of England's website). Additional stress testing is undertaken to assess the impact of extreme stress events.

The stress results provide input to the testing of risk appetite and considerations of capital adequacy and capacity for recovery and resolution planning. Ad hoc stress testing exercises are also undertaken to assess emerging risks and in response to regulatory developments.

The Board Risk Committee reviews all capital and liquidity related stress outputs, including the calculation of indicative capital ratios and the impact of liquidity on the funding plan. In addition to the running of macroeconomic scenarios, the Group's stress testing programme involves undertaking assessments of operational risk, liquidity and financial market disruption scenarios, market risk sensitivities, business specific and reverse stress testing (see relevant risk section for further information on risk specific stress testing). This provides a comprehensive view of the potential impacts arising from the risks to which the Group is exposed.

Stress Testing

Methodology

The Group develops internal scenarios based on key uncertainties for the economic outlook. The stress tests must comply with all legal and regulatory requirements and are subject to a comprehensive review and challenge process.

This is supported by analysis and insight into impacts of the scenarios on customers and business drivers. The engagement of all required risk and control areas is built into the preparation process to ensure appropriate analysis of each risk class's impact upon the business plan is understood and documented.

The methodologies and modelling approach used for stress testing ensures that clear links are shown between the macroeconomic scenarios, the business drivers for each area and the stress testing outputs. All material assumptions used in modelling are documented and justified, with a clearly communicated review and sign-off process. Modelling is supported by expert judgement and is subject to the Model Policy, which includes independent model validation.

Below is an overview of the principal output responsibilities by team.

- Finance and Commercial teams prepare and review stressed business plans including income, margins, costs, lending and deposit volumes;
- technical teams prepare and review risk-related stress outputs, including risk-weighted assets, impairment charges, write-offs and expected loss; and
- Risk teams design stress tests, review the stress submissions and produce a consolidated view of the results, including analysis packs for the Group's senior committees.

Reverse stress testing

Reverse stress testing is used to explore the vulnerabilities of the Group's strategies and plans to extreme adverse events. It also improves contingency planning. The scenarios used in such a stress are those that cause a failure in the business model. Where reverse stress testing reveals plausible scenarios with an unacceptably high risk when considered against risk appetite, the Group will undertake measures to prevent or mitigate that risk as reflected in business and recovery plans.

Governance

Clear accountabilities and responsibilities for stress testing are assigned to senior management and the Risk and Finance functions throughout the Group.

The Executive has primary responsibility for overseeing the development and execution of the Group's stress tests.

The stress test outputs go through a rigorous review and challenge process at business unit level, including sign-off by the Chief Risk Officer. The outputs are then presented for review and challenge, before being approved by the Board.

Risk Management Report

Full Analysis of Risk Classes

Credit risk

Definition

Credit risk is defined as the risk that a borrower or counterparty fails to pay the interest or the capital due on a loan or other financial instrument (both on and off-balance sheet).

Risk appetite

The Group has appetite for high-quality and affordable lending. Credit risk appetite is reported through a comprehensive suite of metrics, supported by triggers, limits and policies.

Exposures

The principal sources of credit risk arise from loans and advances to customers, cash, debt securities and derivatives. The credit risk exposures of the Group are set out on page 159. Credit risk exposures are categorised as retail (secured and unsecured) and wholesale.

In terms of loans and advances, credit risk arises both from amounts lent and commitments to extend credit to a customer. This applies to the secured and unsecured portfolios. The existing overdraft book is a small closed portfolio with overdraft balances anticipated to reduce over time.

Loans and advances expose the Group to customer re-mortgage risk. Re-mortgage risk is the possibility that an outstanding exposure cannot be repaid at its contractual maturity date. If the Group does not wish to re-mortgage the exposure then there is re-mortgage risk if the customer is unable to repay by securing alternative finance. Re-mortgage risk exposures are managed in accordance with the Group's existing credit risk policies, processes and controls. They are not considered to be material given the Group's prudent risk appetite which is designed to be resilient through the cycle.

Where re-mortage risk exists (such as in the interest only retail mortgage portfolio) exposures are minimised through intensive account management and are impaired, where appropriate, with balance sheet provisions raised.

The Group regularly reviews lending practices in line with market conditions and regulatory focus. Growth in buy-to-let lending has been undertaken in a controlled manner, with Board oversight against risk appetite. Buy-to-let lending policy is targeted towards retail customers rather than portfolio landlords, with specific restrictions in place on total exposures by loan amount and number of properties.

Credit risk can also arise from debt securities, derivatives and foreign exchange activities. The Group's wholesale credit risk exposure is reflected on page 173.

Measurement

The Group uses statistical models to measure credit risk exposures. Models are supported by both internal and external data.

The 'probability of default' (that borrowers will not meet their contractual obligations), current exposures, and the likely loss ratio on defaulted obligations are calculated to measure and mitigate credit risk.

Portfolios are assessed by using segmentation for measurement and reporting purposes. Details of the classifications used for asset quality can be found on page 158.

The Group uses Advanced Internal Ratings Based (AIRB) models in measuring the credit risk of secured loans and advances to customers. All retail unsecured and wholesale exposures are measured under the Standardised Approach for regulatory capital.

Page 161 provides details of the Group's approach to the impairment of financial assets. Further details can also be found in note 1 to the financial statements in the Annual Report and Accounts.

Mitigation

The Group uses a range of approaches to mitigate credit risk.

Credit principles and policy

The Risk Function sets out the credit principles and policy for each type of credit risk. Principles and policies are reviewed regularly, and any changes are subject to a review and approval process. Policies, where appropriate, are supported by the lending manual, which defines the responsibilities of underwriters and provides a rule set for credit decisions. These policies and the lending manual define chosen target market and risk acceptance criteria. The Risk Function also uses early warning indicators to help anticipate future areas of concern and allow the Group to take early and proactive mitigating actions. Risk oversight teams monitor credit performance trends, review and challenge exceptions to

Full Analysis of Risk Classes

planned outcomes, and test the adequacy of credit risk infrastructure and governance processes throughout the Group. This includes tracking portfolio performance against an agreed set of key risk indicators. Counterparty exposures are regularly reviewed and appropriate interventions are used where necessary. Oversight and reviews are also undertaken by Risk Assurance and Internal Audit.

Controls over rating systems

The Group has established an Independent Model Validation team that sets common minimum standards. The standards are designed to ensure risk models and associated rating systems are developed consistently, and are of sufficient quality to support business decisions and meet regulatory requirements. Internal rating systems are developed and owned by the Risk Function which takes responsibility for ensuring the validation of the rating systems, supported and challenged by an independent specialist.

Specialist expertise

Credit quality is managed and controlled by specialist units in Operations providing intensive management and control (see Debt management for customers in financial difficulty), maintenance and retention, expertise in documentation for lending and associated products, sector specific expertise, and legal services applicable to the particular market place and product range offered by the business.

Credit decisions may be manually underwritten, where appropriate. This is performed by skilled and competent colleagues acting within their agreed delegated authority.

Stress testing and scenario analysis

The Group's credit portfolios are subjected to regular stress testing, with stress scenario assessments run at various levels of the organisation from Group-led to individual portfolio exercises. For further information on the stress testing process, methodology and governance refer to page 150.

Credit risk assurance and review

A specialist team within Risk Assurance, comprising of experienced credit professionals, is in place to perform credit risk assurance. This team performs independent risk-based reviews providing an assessment of the effectiveness of internal controls and risk management practices. In addition to these 'standard' risk-based reviews, bespoke assignments are also undertaken in response to emerging risks and regulatory requirements.

Additional mitigation for retail customers

The Group uses a variety of lending criteria when assessing applications for mortgages and unsecured lending. The general approval process uses credit acceptance scorecards and involves a review of an applicant's previous credit history using information held by credit reference agencies.

The Group also assesses the affordability of the borrower under stressed scenarios including increased interest rates. In addition, the Group has in place quantitative limits such as maximum limits on the level of borrowing to income and the ratio of borrowing to collateral. Some of these limits relate to internal approval levels and others are hard limits above which the Group will reject the application. The Group also has certain criteria that are applicable to specific products such as applications for a mortgage on a property that is to be let by the applicant.

For residential mortgages, the Group's policy is to accept only standard applications with a loan-to-value (LTV) less than 95%. Applications with a LTV up to 95% are permitted for certain schemes, for example, applications between 90% and 95% LTV are only permitted under the Help to Buy loan guarantee scheme. The Group has maximum % LTV limits which depend upon the loan size. Residential mortgage limits are:

Loan size from	To	Maximum LTV
£1	£500,000	95% (purchase) 90% (remortgage)
£500,001	£1,000,000	80%

Buy-to-let is limited to a maximum of 75% LTV and residential interest only is limited to a maximum of 70% LTV, regardless of loan size.

The Group's approach to underwriting applications for unsecured products takes into account the total unsecured debt held by a customer and its affordability.

The Group rejects any application for an unsecured product where a customer is registered as bankrupt or insolvent, or has a County Court Judgement registered at a credit reference agency used by the Group. In addition, the Group rejects any credit card applicant with excessive levels of secured or unsecured debt.

The Group uses statistically based decisioning techniques (primarily credit scoring models) for its retail portfolios. The Risk Function reviews model effectiveness, while new models and model changes are referred to the appropriate model governance committee for approval.

Risk Management Report

Full Analysis of Risk Classes

Collateral for secured retail and wholesale exposures

The Group maintains guidelines on the acceptability of specific classes of collateral.

The sole collateral type for loans and advances to customers (mortgages) is residential real estate. Property offered as collateral must be of acceptable construction and located in England, Wales, Scotland or Northern Ireland. Title to the property must be good, marketable and free from onerous restrictions and conditions. The Group requires first legal charge over the property offered as collateral and does not accept charges over part of the collateral. The Group does not lend where the collateral is land only.

Collateral held as security for financial assets other than loans and advances is determined by the nature of the instrument. Debt securities, treasury and other bills are generally unsecured, with the exception of asset-backed securities and similar instruments such as covered bonds, which are secured by portfolios of financial assets. Collateral is generally not held against loans and advances to financial institutions, except where a collateral agreement has been entered into under a master netting agreement. Derivative transactions with wholesale counterparties are collateralised under a Credit Support Annex in conjunction with the ISDA Master Agreement.

It is the Group's policy that collateral should always be realistically valued by an appropriately qualified source, independent of both the credit decision process and the customer, at the time of borrowing. Collateral is reviewed on a regular basis and will vary according to the type of lending and collateral involved.

In order to minimise credit loss, the Group may seek additional collateral from a wholesale counterparty as soon as impairment indicators are identified for the relevant wholesale exposures.

The Group considers risk concentrations by collateral providers and collateral type, as appropriate, with a view of ensuring that any potential undue concentrations of risk are identified and suitably managed by changes to strategy, policy and/or business plans (refer to 'Concentration Risk').

Master netting agreements for wholesale exposures

Where it is appropriate, the Group seeks to enter into master netting agreements, or the netting of exposures to a single wholesale counterparty. Master netting agreements do not generally result in an offset of balance sheet assets and liabilities for accounting purposes, as transactions are usually settled on a gross basis. They do reduce the credit risk to the extent that, if an event of default occurs, all amounts with the counterparty are terminated and settled on a net basis. The Group's overall exposure to credit risk on derivative instruments subject to master netting agreements can change substantially within a short period, since this is the net position of all trades under the master netting agreement.

Monitoring

In conjunction with the Risk Function, the business identifies and defines portfolios of credit and related risk exposures and the key benchmarks, behaviours and characteristics by which those portfolios are managed in terms of credit risk exposures. This entails the production and analysis of regular portfolio monitoring reports for review by senior management. The Risk Function in turn produces a review of credit risk throughout the Group, including reports on significant credit exposures, which are presented to the Risk Management Committee and the Board Risk Committee.

The performance of all rating models is monitored on a regular basis to ensure that models provide appropriate risk differentiation capability, the generated ratings remain as accurate and robust as practical, and the models assign appropriate risk estimates to grades/pools. All models are monitored against a series of agreed key performance indicators. In the event that the monitoring identifies material exceptions or deviations from expected outcomes, these will be escalated in accordance with the governance framework.

Debt management for customers in financial difficulty

The Group operates a number of treatments to assist borrowers who are experiencing financial stress. The material elements of these treatments through which the Group has granted a concession, whether temporarily or permanently, are set out as follows.

The Group's aim in offering forbearance and other assistance to retail customers in financial distress is to benefit both the customer and the Group by discharging the Group's regulatory and social responsibilities to support customers and act in their best long-term interests. This allows customer facilities to be brought back into a sustainable position which, for residential mortgages, may also mean keeping customers in their homes. The Group offers a range of tools and assistance

Full Analysis of Risk Classes

to support customers who are encountering financial difficulties. Cases are managed on an individual basis, with the circumstances of each customer considered separately and the action taken judged as being affordable and sustainable for the customer. Operationally, the provision and review of such assistance is controlled by various methods. These include the application of an appropriate policy framework, controls around the execution of policy, regular review of the different treatments to confirm that they remain appropriate, monitoring of customers' performance including the level of payments received, and management visibility of the nature and extent of assistance provided and the associated risk.

Help is provided through the Debt Management Function where tailored repayment programmes can be agreed. Customers are actively supported and referred to free money advice agencies when they have multiple credit facilities, including those at other lenders, which require restructuring.

One component of the management approach is to contact customers showing signs of financial difficulty to discuss their circumstances and offer solutions to prevent their accounts falling into arrears.

Debt management for secured lending

The specific tools available to assist customers vary by product and the customer's status. In defining the treatments offered to customers who have experienced financial distress, the Group distinguishes between the following categories for secured assets:

- payment arrangements: a temporary arrangement for customers in financial distress where arrears accrue at the contractual payment, for example, short-term arrangements to pay less than the contractual payment;
- transfers to interest only: an account change to assist customers through periods of financial difficulty where arrears do not accrue at the original contractual payment. Any arrears existing at the commencement of the arrangement are retained;
- term extensions: a permanent account change for customers in financial distress where the overall term of the mortgage is extended, resulting in a lower contractual monthly payment; and
- discretionary payment holidays: a temporary account change to assist customers through periods of financial difficulty where arrears do not accrue at the original contractual payment. Any arrears existing at the commencement of the arrangement are retained.

To assist customers in financial distress, the Group benefits from Income Support for Mortgage Interest, a UK Government sponsored programme for households. This is a Government medium-term initiative that provides a payment to the Group for certain defined categories of customers (principally those who are unemployed with access to a benefit scheme). Qualifying customers are able to claim for mortgage interest on up to £200,000 of the mortgage. All decisions regarding an individual's eligibility and any amounts payable under the scheme rest solely with the Government. Where this scheme provides borrowers with a state benefit that is used to service the loan, there is no change in the reported status of the loan which is managed and reported in accordance with its original terms.

The Group assesses whether a loan benefiting from this UK Government sponsored programme is impaired using the same accounting policies and practices as it does for loans not benefiting from such a programme. Loans included within the Income Support for Mortgage Interest scheme may be impaired, in accordance with the normal definition of impairment.

The Group is monitoring developments in relation to the ruling by the Northern Ireland courts against capitalisation of arrears in Bank of Scotland versus Rea.

Debt management for unsecured lending

Income and expenditure assessments are undertaken for all customers entering into a long-term repayment plan to ensure that customers are provided with a sustainable and affordable solution that allows customers a realistic opportunity to repay their debt in the short to medium-term. In addition, the Group will signpost customers to contact debt management companies (such as Citizens Advice Bureau, Stepchange and Payplan). These companies do not charge any fees and will offer advice to customers as well as work with creditors to agree affordable repayment plans. Understanding what has changed and establishing the customers' current and future financial situation is imperative to ensuring that the right level of support is offered and that customers receive the appropriate solution to help them manage their debt when in financial difficulty.

Risk Management Report

Full Analysis of Risk Classes

Forbearance and provisioning

The Group measures the success of forbearance schemes for secured loans. This is based upon the proportion of customers who remain neither past due nor impaired or repay their loan fully over the 12 months following the exit from a forbearance treatment. For temporary treatments, 100% of customers accepting reduced payment arrangements have remained within contractual terms following the end of their treatment, and are either fully up to date or had redeemed their loan as at 31 December 2015. For permanent treatments, 94% of customers who have accepted interest only concessions, 96% of customers who have had a discretionary payment holiday and 95% of customers who have accepted term extensions, remained within contractual terms following the end of their treatment as at 31 December 2015.

The Group classifies a retail account as forborne at the time a customer in financial difficulty is granted a concession. Accounts are classified as forborne only for the period of time which the exposure is known to be, or may still be, in financial difficulty. Where temporary forbearance is granted, exit criteria are applied to include accounts until they are known to no longer be in financial difficulty.

Where the treatment involves a permanent change to the contractual basis of the customer's account, such as conversion to interest only or term extension, the Group classifies the balance as forborne for a period of 12 months, after which no distinction is made between these accounts and others where no change has been made.

The Group's approach is to ensure that provisioning models, supported by management judgement, appropriately reflect the incurred loss risk of exposures. The Group uses sophisticated behavioural scoring to assess customers' credit risk. The underlying behavioural scorecards consider many different characteristics of customer behaviour, both static and dynamic, from internal sources and also from credit bureau data, including characteristics that may identify when a customer has been in arrears on products held with other firms. Hence, these models take a range of potential indicators of customer financial distress into account.

The performance of provision models is monitored and challenged on an ongoing basis in line with the Retail Credit Provisioning Policy. The models are also regularly recalibrated to reflect up to date customer behaviour and market conditions. Specifically, regular detailed analysis of modelled provision outputs is undertaken to demonstrate that the risk of forbearance or other similar activities is recognised, that the outcome period adequately captures the risk and that the underlying risk is appropriately reflected. Where this is not the case, additional provisions are applied to capture the risk.

Forbearance provisioning for secured lending

At 31 December 2015, £259.5 million (2014: £267.5 million) of retail secured loans and advances were currently, or recently, subject to forbearance.

Collective impairment assessment of retail secured loans subject to forbearance: Loans which are forborne are grouped with other assets with similar risk characteristics and assessed collectively for impairment. The loans are not considered as impaired loans unless they meet the Group's definition of an impaired asset.

Forbearance provisioning for unsecured lending

At 31 December 2015, total retail unsecured loans and advances benefiting from forbearance totalled £10.7 million (2014: £12.9 million).

Collective impairment assessment of retail unsecured loans and advances subject to forbearance: Credit risk provisioning for the retail unsecured portfolio is undertaken on a collective basis, except for fraud cases which are fully provided for. The approach used is based on roll rates for various behavioural and arrears status segments, measuring the likelihood of default and the probability of charge-off given default.

Following the migration of the credit card portfolio, the Group widened its definition of forbearance. The migration of the credit card portfolio to the Group's infrastructure has allowed an improvement to management information and better identification of individual customer circumstances.

Full Analysis of Risk Classes

Credit risk portfolio 31 December 2015

Overview

- impairment provisions increased 30% to £39.9 million as at 31 December 2015 (2014: £30.6 million);
- impairment assets as a percentage of loans and advances to customers remained stable at 0.4% as at 31 December 2015 (2014: 0.5%); and
- there were no wholesale impairment provisions as at 31 December 2015.

The table below shows total credit exposures.

	Secured		Unsecured		Wholesale		
	Residential mortgage loans £m	Residential buy-to-let mortgage loans £m	Credit cards £m	Overdrafts £m	Treasury assets £m	Derivative exposures £m	Total £m
2015 (audited)							
Total gross loans and advances to customers	**21,060.3**	**4,401.9**	**1,609.8**	**0.2**	**–**	**–**	**27,072.2**
Loans and advances to banks	**–**	**–**	**–**	**–**	**614.5**		**614.5**
Cash and balances at central banks	**–**	**–**	**–**	**–**	**888.6**	**–**	**888.6**
Debt securities classified as loans and receivables	**–**	**–**	**–**	**–**	**1.1**	**–**	**1.1**
Available-for-sale financial assets	**–**	**–**	**–**	**–**	**1,296.9**	**–**	**1,296.9**
Gross positive fair value of derivative assets	**–**	**–**	**–**	**–**	**–**	**82.3**	**82.3**
Total	**21,060.3**	**4,401.9**	**1,609.8**	**0.2**	**2,801.1**	**82.3**	**29,955.6**

Risk Management Report

Full Analysis of Risk Classes

	Secured		Unsecured		Wholesale		
	Residential mortgage loans £m	Residential buy-to-let mortgage loans £m	Credit cards £m	Overdrafts £m	Treasury assets £m	Derivative exposures £m	Total £m
2014 (audited)							
Total gross loans and advances to customers	18,759.5	3,135.6	1,121.1	0.2	–	–	23,016.4
Loans and advances to banks excluding Bank of England	–	–	–	–	720.5	–	720.5
Cash and balances at central banks	–	–	–	–	851.3		851.3
Debt securities classified as loans and receivables	–	–	–	–	8.6	–	8.6
Available-for-sale financial assets	–	–	–	–	1,539.6		1,539.6
Gross positive fair value of derivative assets	–	–	–	–	–	101.2	101.2
Total	**18,759.5**	**3,135.6**	**1,121.1**	**0.2**	**3,120.0**	**101.2**	**26,237.6**

Credit quality of assets

Loans and receivables

The Group defines three classifications of credit quality (low risk, medium risk and higher risk) for all credit exposures. These are based on the following criteria for the different credit risk exposure types.

Secured credit exposures are segmented according to the credit quality classification and a point in time probability of default (PD). The point in time PD is an internal parameter used within the Group's AIRB capital models which aims to estimate the probability of default over the next 12 months based on account characteristics and customer behavioural data. Default occurs where a borrower has missed six months of mortgage repayments or the borrower is deemed to be unlikely to repay their loan. Exposures are categorised as:

- higher risk where assets are past due or have a point in time PD greater than 2%;
- medium risk where assets are not past due and have a PD greater than 0.8% and less than or equal to 2%; and
- low risk where assets are not past due and have a PD less than or equal to 0.8%.

Unsecured exposures are categorised as:

- higher risk where assets are past due;
- medium risk where assets are currently not past due and benefiting from a forbearance solution; and
- low risk where assets are neither past due nor in forbearance.

Wholesale credit exposures are assessed by reference to credit rating. The Group's wholesale exposures are investment grade and therefore classified as low risk.

Further asset quality categorisation is disclosed on page 161, which reflects the impairment status of assets.

No wholesale loans and receivables credit exposures are past due nor impaired as at 31 December 2015 or 2014.

Full Analysis of Risk Classes

Maximum credit exposure

The maximum credit risk exposure of the Group in the event of other parties failing to perform their obligations is detailed below. No account is taken of any collateral held, other credit enhancements or provisions for impairment.

The maximum credit risk exposure for off-balance sheet items relates to applications that have been approved and have not yet been drawn by the customer and undrawn loan commitments (pipeline). These commitments represent agreements to lend in the future and may be decreased or removed by the Group, subject to product notice requirements.

	Low risk £m	Medium risk £m	Higher risk £m	Total exposures £m	Low risk %	Medium risk %	Higher risk %
2015 (audited) **On-balance sheet**							
Wholesale							
Cash and balances at central banks	888.6	–	–	888.6	100.0	–	–
Debt securities classified as loans and receivables	1.1	–	–	1.1	100.0	–	–
Available-for-sale financial assets	1,296.9	–	–	1,296.9	100.0	–	–
Loan and advances to banks	614.5	–	–	614.5	100.0	–	–
Derivative financial instruments	82.3	–	–	82.3	100.0	–	–
Retail							
Gross loans and advances to customers – secured	22,916.7	1,652.7	892.8	25,462.2	90.0	6.5	3.5
Gross loans and advances to customers – unsecured	1,579.7	2.9	27.4	1,610.0	98.1	0.2	1.7
Total on-balance sheet	27,379.8	1,655.6	920.2	29,955.6	91.4	5.5	3.1
Off-balance sheet							
Loan commitments (pipeline and undrawn commitments)	4,479.8	–	–	4,479.8	100.0	–	–

Risk Management Report

Full Analysis of Risk Classes

	Low risk £m	Medium risk £m	Higher risk £m	Total exposures £m	Low risk %	Medium risk %	Higher risk %
2014 (audited) **On-balance sheet**							
Wholesale							
Cash and balances at central banks	851.3	–	–	851.3	100.0	–	–
Debt securities classified as loans and receivables	8.6	–	–	8.6	100.0	–	–
Available-for-sale financial assets	1,539.6	–	–	1,539.6	100.0	–	–
Loan and advances to banks	720.5	–	–	720.5	100.0	–	–
Derivative financial instruments	101.2	–	–	101.2	100.0	–	–
Retail							
Gross loans and advances to customers – secured	19,636.3	1,574.5	684.3	21,895.1	89.7	7.2	3.1
Gross loans and advances to customers – unsecured[1]	1,090.7	3.2	27.4	1,121.3	97.3	0.3	2.4
Total on-balance sheet	**23,948.2**	**1,577.7**	**711.7**	**26,237.6**	**91.3**	**6.0**	**2.7**
Off-balance sheet							
Loan commitments (pipeline and undrawn commitments)	3,694.2	–	–	3,694.2	100.0	–	–

1 The December 2014 forbearance balance was restated to reflect a change in the definition to include customers categorised as in hardship and on a payment plan or vulnerable.

Loans and advances to customers comprise:

	2015	2014
(audited)	**£m**	£m
Advances secured on residential property not subject to securitisation	**17,389.9**	15,631.2
Advances secured on residential property subject to securitisation	**3,670.4**	3,128.3
Total advances secured on residential property	**21,060.3**	18,759.5
Residential buy-to-let loans not subject to securitisation	**4,401.9**	3,135.6
Total loans and advances to customers secured on residential property	**25,462.2**	21,895.1
Impairment allowance-secured	**(8.7)**	(7.6)
Loans and advances-secured	**25,453.5**	21,887.5
Credit cards	**1,609.8**	1,121.1
of which relates to the fair value of expected losses on acquired assets	**–**	*(5.4)*
Overdrafts	**0.2**	0.2
Unsecured receivables not subject to securitisation	**1,610.0**	1,121.3
Impairment allowance – unsecured	**(31.2)**	(23.0)
Loans and advances – unsecured	**1,578.8**	1,098.3
Total loans and advances to customers excluding portfolio hedging	**27,032.3**	**22,985.8**

Full Analysis of Risk Classes

The mortgage portfolio has grown by 16% (£3.6 billion) during 2015. Buy-to-let loans grew by 40% (£1.3 billion) to £4.4billion, accounting for 17% of total secured loans (2014: 14%). This increase is in line with growth in the private rental sector and buy-to-let mortgage lending in the market. Growth in buy-to-let lending has been undertaken in a controlled manner, with the intention of moving BTL mix broadly in line with the market average.

Secured impairment allowances increased from £7.6 million to £8.7 million during 2015 in line with portfolio growth. Unsecured impairment provisions increased by £8.2 million to £31.2 million as a result of the unwinding of the fair value adjustment (£5.4 million unwound during 2015 of the original £5.9 million adjustment) for the credit card assets transferred onto the Group's balance sheet in November 2014 (accounts acquired and on MBNA systems from January 2013), and by the increase in new lending.

Credit risk categorisation	Description
Neither past due nor impaired	Loans that are not in arrears and which do not meet the impaired asset definition. This segment can include assets subject to forbearance solutions.
Neither past due nor impaired and in forbearance	Loans that are categorised as neither past due nor impaired, and are currently subject to one of the defined forbearance solutions.
Past due and not impaired	Loans that are in arrears or where there is objective evidence of impairment and the asset does not meet the definition of impaired assets, as the expected recoverable amount exceeds the carrying amount. This category is not applicable for unsecured lending.
Arrears	For secured lending, where the customer's payment shortfall exceeds 1% of the current monthly contractual payment amount. For unsecured lending, customers are classified as in arrears at one day past due.
Impaired assets	Loans that are in arrears or where there is objective evidence of impairment, including changes in customer behaviour or circumstances, and where the carrying amount of the loan exceeds the expected recoverable amount. Unsecured lending assets are treated as impaired at one day past due. All fraud and operational risk loans are categorised as impaired irrespective of the expected recoverable amount.

The credit quality of retail assets is detailed in the tables below.

	Secured				Unsecured				Total	
	Residential mortgage loans		Residential buy-to-let mortgage loans		Credit cards		Overdrafts			
	£m	%	£m	%	£m	%	£m	%	£m	%
2015 (audited)										
Neither past due nor impaired	**20,837.5**	**98.9**	**4,379.9**	**99.5**	**1,582.4**	**98.3**	**0.2**	**100.0**	**26,800.0**	**99.0**
– of which in receipt of forbearance[1]	*238.6*	*1.1*	*8.8*	*0.2*	*2.9*	*0.2*	–	–	*250.3*	*0.9*
Past due and not impaired	**145.2**	**0.7**	**15.0**	**0.3**	–	–	–	–	**160.2**	**0.6**
Impaired	**77.6**	**0.4**	**7.0**	**0.2**	**27.4**	**1.7**	–	–	**112.0**	**0.4**
Total	**21,060.3**	**100.0**	**4,401.9**	**100.0**	**1,609.8**	**100.0**	**0.2**	**100.0**	**27,072.2**	**100.0**

1 This category reflects accounts which are neither past due nor impaired and subject to forbearance solutions. Accounts in this category are also included in the neither past due nor impaired categorisation.

Risk Management Report

Full Analysis of Risk Classes

	Secured				Unsecured				Total	
	Residential mortgage loans		Residential buy-to-let mortgage loans		Credit cards		Overdrafts			
	£m	%	£m	%	£m	%	£m	%	£m	%
2014 (audited)										
Neither past due nor impaired	18,508.0	98.6	3,110.4	99.2	1,093.7	97.6	0.2	100.0	22,712.3	98.6
– of which in receipt of forbearance[1]	*241.7*	*1.3*	*7.2*	*0.2*	*3.2*	*0.3*	–	–	*252.1*	*1.1*
Past due and not impaired	182.6	1.0	17.6	0.6	–	–	–	–	200.2	0.9
Impaired	68.9	0.4	7.6	0.2	27.4	2.4	–	–	103.9	0.5
Total	**18,759.5**	**100.0**	**3,135.6**	**100.0**	**1,121.1**	**100.0**	**0.2**	**100.0**	**23,016.4**	**100.0**

1 This category reflects accounts which are neither past due nor impaired and subject to forbearance solutions. Accounts in this category are also included in the neither past due nor impaired categorisation. The December 2014 forbearance balance was restated to reflect a change in the definition to include customers categorised as in hardship and on a payment plan or vulnerable.

The criteria the Group use to determine that there is objective evidence of impairment are disclosed on page 161. All loans, where specific circumstances indicate that a loss is likely to be incurred (for example, mortgage accounts which have entered possession or loans where fraud has been confirmed), are individually assessed for impairment by reviewing expected future cash flows including those that could arise from the realisation of security.

Loans and advances which are neither past due nor impaired

Neither past due nor impaired balances account for 99.0% of the total portfolio (2014: 98.6%). This improvement is driven by new lending in the period, along with an overall reduction of customers in arrears.

There has been an increase in the higher risk balances within this categorisation due to accounts which have moved from being past due, and therefore remain to hold a higher probability of default.

The table below shows the details of the credit quality for neither past due nor impaired loans.

	Residential mortgage loans		**Residential buy-to-let mortgage loans**		**Total**	
	£m	**%**	**£m**	**%**	**£m**	**%**
2015 (audited)						
PD by internal ratings						
Low risk	**18,681.1**	**89.6**	**4,235.6**	**96.7**	**22,916.7**	**90.8**
Medium risk	**1,519.0**	**7.3**	**133.7**	**3.1**	**1,652.7**	**6.6**
Higher risk	**637.4**	**3.1**	**10.6**	**0.2**	**648.0**	**2.6**
Total neither past due nor impaired	**20,837.5**	**100.0**	**4,379.9**	**100.0**	**25,217.4**	**100.0**

Full Analysis of Risk Classes

	Residential mortgage loans		Residential buy-to-let mortgage loans		Total	
	£m	%	£m	%	£m	%
2014 (audited)						
PD by internal ratings						
Low risk	16,597.7	89.7	3,038.6	97.6	19,636.3	90.8
Medium risk	1,507.5	8.1	67.0	2.2	1,574.5	7.3
Higher risk	402.8	2.2	4.8	0.2	407.6	1.9
Total neither past due nor impaired	**18,508.0**	**100.0**	**3,110.4**	**100.0**	**21,618.4**	**100.0**

Loans and advances which are past due and not impaired

The balance of mortgages which are past due and not impaired totalled £160.2 million at 31 December 2015. There are no past due and not impaired balances relating to unsecured loans as these are included in the impaired definition. This represents a 20% (£40.0 million) decrease from 2014, attributable to improved arrears performance. These assets now represent 0.6% of secured loans (2014: 0.9%).

	Residential mortgage loans		**Residential buy-to-let mortgage loans**		**Total**	
	£m	**%**	**£m**	**%**	**£m**	**%**
2015 (audited)						
Up to one month	**44.4**	**30.6**	**4.3**	**28.7**	**48.7**	**30.4**
One to three months	**63.5**	**43.7**	**8.3**	**55.3**	**71.8**	**44.8**
Three to six months	**24.1**	**16.6**	**1.3**	**8.7**	**25.4**	**15.9**
Over six months	**13.2**	**9.1**	**1.1**	**7.3**	**14.3**	**8.9**
Total past due and not impaired	**145.2**	**100.0**	**15.0**	**100.0**	**160.2**	**100.0**

	Residential mortgage loans		Residential buy-to-let mortgage loans		Total	
	£m	%	£m	%	£m	%
2014 (audited)						
Up to one month	59.3	32.5	5.2	29.5	64.5	32.2
One to three months	72.1	39.5	8.2	46.6	80.3	40.1
Three to six months	29.6	16.2	2.6	14.8	32.2	16.1
Over six months	21.6	11.8	1.6	9.1	23.2	11.6
Total past due and not impaired	**182.6**	**100.0**	**17.6**	**100.0**	**200.2**	**100.0**

Risk Management Report

Full Analysis of Risk Classes

Impaired assets

The tables below show the movement of impaired loan balances during 2015 and 2014.

	Secured		Unsecured		Wholesale		
	Residential mortgage loans £m	**Residential buy-to-let mortgage loans £m**	**Credit cards £m**	**Overdrafts £m**	**Treasury assets £m**	**Derivative exposures £m**	**Total £m**
2015 (audited)							
As at 1 January 2015	**68.9**	**7.6**	**27.4**	**–**	**–**	**–**	**103.9**
Classified as impaired during the year	**174.9**	**22.2**	**81.9**	**–**	**–**	**–**	**279.0**
Transferred from impaired to unimpaired	**(151.2)**	**(21.6)**	**(42.7)**	**–**	**–**	**–**	**(215.5)**
Amounts written off	**(1.7)**	**(0.2)**	**(26.0)**	**–**	**–**	**–**	**(27.9)**
Repayments	**(13.3)**	**(1.0)**	**(13.2)**	**–**	**–**	**–**	**(27.5)**
As at 31 December 2015	**77.6**	**7.0**	**27.4**	**–**	**–**	**–**	**112.0**

	Secured		Unsecured		Wholesale		
	Residential mortgage loans	Residential buy-to-let mortgage loans	Credit cards	Overdrafts	Treasury assets	Derivative exposures	Total
2014 (audited)	£m	£m	£m	£m	£m	£m	£m
As at 1 January 2014	103.2	8.5	26.6	–	–	–	138.3
Classified as impaired during the year	121.6	14.5	77.0	–	–	–	213.1
Transferred from impaired to unimpaired	(136.5)	(13.7)	(39.4)	–	–	–	(189.6)
Amounts written off	(1.1)	(0.1)	(27.6)	–	–	–	(28.8)
Repayments	(18.3)	(1.6)	(9.2)	–	–	–	(29.1)
As at 31 December 2014	**68.9**	**7.6**	**27.4**	**–**	**–**	**–**	**103.9**

Total impaired assets increased by £8.1 million in the year to 31 December 2015. The increase in impaired asset balances on the secured portfolio is a result of a higher rate of discount cost observed on sold possessions, which have reduced the estimated recoverable loan amount of assets in this category. Observed discount costs are based on a low volume of possession sales during 2015 which have reduced to 47 cases (2014: 63). Possession stock reduced to 12 cases at 31 December 2015 from 18 cases in 2014. Despite this, secured impaired assets as a proportion of total secured loans remain stable at 0.3%.

Full Analysis of Risk Classes

An analysis of impaired assets by overdue term and assets where the borrower's property is in possession is provided in the table below.

	Residential mortgage loans		Residential buy-to-let mortgage loans		Credit cards		Overdrafts		Total	
	£m	%	£m	%	£m	%	£m	%	£m	%
2015 (audited)										
Up to one month	**50.6**	**65.1**	**4.5**	**64.3**	**11.8**	**43.1**	–	–	**66.9**	**59.7**
One to three months	**13.7**	**17.7**	**1.4**	**20.0**	**7.6**	**27.7**	–	–	**22.7**	**20.3**
Three to six months	**5.2**	**6.7**	**0.3**	**4.3**	**7.7**	**28.1**	–	–	**13.2**	**11.8**
Over six months	**7.2**	**9.3**	**0.7**	**10.0**	**0.3**	**1.1**	–	–	**8.2**	**7.3**
Possession	**0.9**	**1.2**	**0.1**	**1.4**	–	–	–	–	**1.0**	**0.9**
Total impaired assets	**77.6**	**100.0**	**7.0**	**100.0**	**27.4**	**100.0**	–	–	**112.0**	**100.0**

	Residential mortgage loans		Residential buy-to-let mortgage loans		Credit cards		Overdrafts		Total	
	£m	%	£m	%	£m	%	£m	%	£m	%
2014 (audited)										
Up to one month	44.1	64.0	4.0	52.7	11.0	40.1	–	–	59.1	56.9
One to three months	10.3	14.9	2.3	30.3	8.0	29.2	–	–	20.6	19.8
Three to six months	4.5	6.5	0.3	3.9	8.4	30.7	–	–	13.2	12.7
Over six months	9.0	13.1	0.7	9.2	–	–	–	–	9.7	9.3
Possession	1.0	1.5	0.3	3.9	–	–	–	–	1.3	1.3
Total impaired assets	**68.9**	**100.0**	**7.6**	**100.0**	**27.4**	**100.0**	–	–	**103.9**	**100.0**

Risk Management Report

Full Analysis of Risk Classes

The tables below show impaired assets and impairment provisions.

	Gross balances £m	Impaired balances £m	Impaired balances as a % of gross balances	Impairment provisions £m	Impairment provisions as a % of impaired balances
2015 (audited)					
Residential mortgage loans	**21,060.3**	**77.6**	**0.4**	**7.7**	**9.9**
Residential buy-to-let mortgage loans	**4,401.9**	**7.0**	**0.2**	**1.0**	**14.3**
Total secured	**25,462.2**	**84.6**	**0.3**	**8.7**	**10.3**
Credit cards	**1,609.8**	**27.4**	**1.7**	**31.1**	**113.5**
Overdrafts	**0.2**	**–**	**–**	**0.1**	**–**
Total unsecured	**1,610.0**	**27.4**	**1.7**	**31.2**	**113.9**
Wholesale treasury assets	**2,801.1**	**–**	**–**	**–**	**–**
Wholesale derivative exposures	**82.3**	**–**	**–**	**–**	**–**
Total wholesale	**2,883.4**	**–**	**–**	**–**	**–**
Total	**29,955.6**	**112.0**	**0.4**	**39.9**	**35.6**

	Gross balances £m	Impaired balances £m	Impaired balances as a % of gross balances	Impairment provisions £m	Impairment provisions as a % of impaired balances
2014 (audited)					
Residential mortgage loans	18,759.5	68.9	0.4	6.2	9.0
Residential buy-to-let mortgage loans	3,135.6	7.6	0.2	1.4	18.4
Total secured	21,895.1	76.5	0.3	7.6	9.9
Credit cards	1,121.1	27.4	2.4	22.9	83.6
Overdrafts	0.2	–	–	0.1	–
Total unsecured	1,121.3	27.4	2.4	23.0	83.9
Wholesale treasury assets	3,120.0	–	–	–	–
Wholesale derivative exposures	101.2	–	–	–	–
Total wholesale	**3,221.2**	**–**	**–**	**–**	**–**
Total	**26,237.6**	**103.9**	**0.4**	**30.6**	**29.5**

Impairment provisions:

- have increased by £1.1 million for secured loans in line with portfolio growth; and
- have increased by £8.2 million for unsecured loans, of which £5.4 million was attributable to unwinding the fair value adjustment described on page 161.

Full Analysis of Risk Classes

Impairment provisions as a percentage of impaired loans:

- for secured loans have increased from 9.9% to 10.3% despite an increase in impaired loans; and
- for unsecured loans have increased from 83.9% to 113.9% as result of the aforementioned unwinding of the fair value adjustment, showing a stable underlying performance.

The table below shows the movement of impairment provisions during the year.

	Secured		Unsecured		Wholesale		
(audited)	Residential mortgage loans £m	Residential buy-to-let mortgage loans £m	Credit cards £m	Overdrafts £m	Treasury assets £m	Derivative exposures £m	Total £m
At 1 January 2014	**7.0**	**0.6**	**27.0**	**0.1**	**–**	**–**	**34.7**
Advances written off	**(1.1)**	**(0.1)**	**(27.6)**	**–**	**–**	**–**	**(28.8)**
Gross charge to the income statement[1]	**0.3**	**0.9**	**23.5**	**–**			**24.7**
As 31 December 2014	**6.2**	**1.4**	**22.9**	**0.1**			**30.6**
Amounts written off during the year	**(1.7)**	**(0.2)**	**(26.0)**	**–**			**(27.9)**
Gross charge to the income statement[1]	**3.2**	**(0.2)**	**34.2**	**–**	**–**	**–**	**37.2**
As at 31 December 2015	**7.7**	**1.0**	**31.1**	**0.1**	**–**	**–**	**39.9**

1 The net charge to the income statement in 2015 was £30.3 million (2014: £15.8 million). The difference between the gross and net charge represents sales of credit card receivables which had previously been written-off resulting in net recoveries of £6.9 million (2014: £8.9 million).

The Group's impairment charge increased from £24.7 million in 2014 to £37.2 million as at 31 December 2015.

Collateral held as security for financial assets

A general description of collateral held as security in respect of financial instruments is provided on page 154. The Group holds collateral against loans and receivables on the mortgage portfolio. Quantitative and, where appropriate, qualitative information is provided in respect of this collateral on page 170.

Loans and receivables to customers

The Group holds collateral in respect of loans and advances to customers as set out on page 154. The Group does not hold collateral against debt securities, comprising asset-backed securities and corporate and other debt securities, which are classified as loans and receivables.

Risk Management Report

Full Analysis of Risk Classes

The table below shows retail secured loan-to-value (LTV) % – indexed value at financial period end.

2015 (audited)	**Residential mortgage loans** £m	**Residential mortgage loans** %	**Residential buy-to-let mortgage loans** £m	**Residential buy-to-let mortgage loans** %	**Total** £m	**Total** %
<50%	**8,125.8**	**38.6**	**1,443.5**	**32.8**	**9,569.3**	**37.6**
50%-<60%	**4,680.7**	**22.2**	**1,202.9**	**27.3**	**5,883.6**	**23.1**
60%-<70%	**4,026.2**	**19.1**	**1,069.7**	**24.3**	**5,095.9**	**20.0**
70%-<80%	**2,247.7**	**10.7**	**680.5**	**15.5**	**2,928.2**	**11.5**
80%-<90%	**1,720.1**	**8.2**	**3.4**	**0.1**	**1,723.5**	**6.8**
90%-<100%	**250.4**	**1.2**	**1.4**	**–**	**251.8**	**1.0**
>100%	**9.4**	**–**	**0.5**	**–**	**9.9**	**–**
Total	**21,060.3**	**100.0**	**4,401.9**	**100.0**	**25,462.2**	**100.0**
Average loan-to-value[1] of stock – indexed		**54.9%**		**55.4%**		**55.0%**
Average loan-to-value of new business		**69.8%**		**62.7%**		**68.0%**

1 The average loan-to-value of stock and new business is balance weighted.

2014 (audited)	Residential mortgage loans £m	Residential mortgage loans %	Residential buy-to-let mortgage loans £m	Residential buy-to-let mortgage loans %	Total £m	Total %
<50%	6,252.0	33.3	909.9	29.0	7,161.9	32.7
50%-<60%	4,649.9	24.8	978.3	31.2	5,628.2	25.7
60%-<70%	4,132.2	22.0	842.4	26.9	4,974.6	22.7
70%-<80%	2,464.8	13.1	396.0	12.6	2,860.8	13.1
80%-<90%	1,064.3	5.7	5.3	0.2	1,069.6	4.9
90%-<100%	180.9	1.0	2.4	0.1	183.3	0.8
>100%	15.4	0.1	1.3	–	16.7	0.1
Total	**18,759.5**	**100.0**	**3,135.6**	**100.0**	**21,895.1**	**100.0**
Average loan-to-value[1] of stock – indexed		55.8%		55.6%		55.7%
Average loan-to-value of new business		68.4%		61.3%		66.9%

1 The average loan-to-value of stock and new business is balance weighted.

Average indexed LTVs on the book have decreased marginally by 0.7% as at 31 December 2015, reflecting the impact of house price movements reported between Q4 2014 and Q3 2015 for all UK regions.

The average LTV for new business has increased to 68.0% as at 31 December 2015 (2014: 66.9%). This has been partly driven by more than 3,500 new mortgages written under the government's Help to Buy schemes in 2015.

Full Analysis of Risk Classes

Details of the fair value of the property collateral held against retail secured loans are provided in the table below.

	Residential mortgage loans		**Residential buy-to-let mortgage loans**		**Total**	
	£m	**%**	**£m**	**%**	**£m**	**%**
2015[1] (audited)						
Neither past due nor impaired	**20,836.9**	**100.0**	**4,379.8**	**100.0**	**25,216.7**	**100.0**
– of which in receipt of forbearance	*238.6*	*100.0*	*8.8*	*100.0*	*247.4*	*100.0*
Past due and not impaired	**145.2**	**100.0**	**15.0**	**100.0**	**160.2**	**100.0**
Impaired	**77.3**	**99.6**	**7.0**	**100.0**	**84.3**	**99.6**
– of which in possession	*0.9*	*100.0*	*0.1*	*100.0*	*1.0*	*100.0*
Total	**21,059.4**	**100.0**	**4,401.8**	**100.0**	**25,461.2**	**100.0**

1 Some segments may look fully collateralised due to immaterial balances in negative equity. Due to rounding these do not change the overall collateralised percentage shown.

Collateral held in relation to secured loans is capped at the amount outstanding on an individual loan basis. The percentages in the previous table represent the value of collateral, capped at loan amount, divided by the total loan amount in each category.

	Residential mortgage loans		Residential buy-to-let mortgage loans		Total	
	£m	%	£m	%	£m	%
2014[1] (audited)						
Neither past due nor impaired	18,506.6	100.0	3,110.2	100.0	21,616.8	100.0
– of which in receipt of forbearance	*241.7*	*100.0*	*7.2*	*100.0*	*248.9*	*100.0*
Past due and not impaired	182.6	100.0	17.6	100.0	200.2	100.0
Impaired	68.4	99.3	7.6	100.0	76.0	99.3
– of which in possession	*1.0*	*100.0*	*0.3*	*100.0*	*1.3*	*100.0*
Total	**18,757.6**	**100.0**	**3,135.4**	**100.0**	**21,893.0**	**100.0**

1 Some segments may look fully collateralised due to immaterial balances in negative equity. Due to rounding these do not change the overall collateralised percentage shown.

Risk Management Report

Full Analysis of Risk Classes

The tables below show mortgages in negative equity. The value represents the excess between the mortgage balance and collateral value for mortgages where indexed LTV is greater than 100%.

The proportion of secured balances in negative equity has fallen below 0.1% at 31 December 2015 (2014: 0.1%). This relates to £9.9 million of asset balances in the mortgage portfolio that are exposed to negative equity (2014: £16.7 million). The amount of negative equity has decreased from £2.1 million at 31 December 2014 to £1.0 million as at 31 December 2015 as a result of positive house price movements observed in the portfolio.

	Residential mortgage loans £m	Residential buy-to-let mortgage loans £m	Total £m
2015 (audited)			
Neither past due nor impaired	**0.6**	**0.1**	**0.7**
– of which in receipt of forbearance	**–**	**–**	**–**
Past due and not impaired	**–**	**–**	**–**
Impaired	**0.3**	**–**	**0.3**
– of which in possession	**–**	**–**	**–**
Total	**0.9**	**0.1**	**1.0**

	Residential mortgage loans £m	Residential buy-to-let mortgage loans £m	Total £m
2014 (audited)			
Neither past due nor impaired	1.4	0.2	1.6
– of which in receipt of forbearance	–	–	–
Past due and not impaired	–	–	–
Impaired	0.5	–	0.5
– of which in possession	–	–	–
Total	**1.9**	**0.2**	**2.1**

Possessions

The Group works with customers who have difficulty paying their mortgages, and will only repossess a property when all other possibilities have been exhausted. Where accounts have been repossessed, the Group will obtain the best price that might reasonably be paid taking into account factors such as property and market conditions.

The Group uses external asset management specialists to realise the value as soon as practicable to settle indebtedness. Any surplus funds are returned to the borrower or are otherwise dealt with in accordance with appropriate insolvency regulations.

Full Analysis of Risk Classes

	2015		2014	
Possessions as a percentage of total book (number of properties)	**Number**	**%**	Number	%
Properties in possession	**12.0**	**0.01**	18.0	0.01
CML industry average[1]	**3,200.0**	**0.03**	**6,400.0**	**0.06**

1 CML possession as at Q4 2015. The CML industry average includes banks with portfolios significantly larger than Virgin Money that drive up the industry average, so the percentage comparisons are more meaningful than the pure number comparisons.

Interest only mortgages

The Group provides interest only mortgages to customers, whereby payments made by the customer comprise interest for the term of the mortgage, with the customer responsible for repaying the principal outstanding at the end of the loan term. The Group's exposure to residential interest only mortgages for the year to 31 December 2015 has reduced, accounting for 33.1% of total secured balances, compared to 36.9% at 31 December 2014.

The table below provides details of balances which are on an interest only basis, analysed by maturity. This includes the interest only balances for loans on a part and part repayment basis.

2015 (audited)	**Residential mortgage loans £m**	**Residential buy-to-let mortgage loans £m**	**Total £m**
Term expired (still open)	**19.1**	**0.7**	**19.8**
Due within 2 years	**172.4**	**15.7**	**188.1**
Due after 2 years and before 5 years	**411.6**	**57.6**	**469.2**
Due after 5 years and before 10 years	**1,017.7**	**488.1**	**1,505.8**
Due after more than 10 years	**3,173.2**	**3,068.6**	**6,241.8**
Total	**4,794.0**	**3,630.7**	**8,424.7**
% of total secured loans and advances to customers	**22.8**	**82.5**	**33.1**

2014 (audited)	Residential mortgage loans £m	Residential buy-to-let mortgage loans £m	Total £m
Term expired (still open)	19.3	0.6	19.9
Due within 2 years	115.8	8.7	124.5
Due after 2 years and before 5 years	434.5	51.8	486.3
Due after 5 years and before 10 years	1,057.2	385.3	1,442.5
Due after more than 10 years	3,880.3	2,123.1	6,003.4
Total	5,507.1	2,569.5	8,076.6
% of total secured loans and advances to customers	29.4	81.9	36.9

Risk Management Report

Full Analysis of Risk Classes

Following a pilot exercise in 2014, a process is now in place to ensure that contact is made with customers who have an interest only mortgage scheduled to mature before the end of 2020. These customers are contacted each year to ask if their repayment strategy remains on track to repay the interest only mortgage loan in full at the end of the agreed term. If they are not on track, they are encouraged to make contact to discuss their options.

Interest only balances due to mature in the next two years represent 2.2% of total interest only balances, totalling £188.1 million at 31 December 2015. Treatment strategies exist to help customers who may not be able to repay the full amount of principal balance at maturity. Of residential interest only mortgages which have missed the payment of principal at the end of term, £19.8 million remain at 31 December 2015 (2014: £19.9 million).

All expired term balances are categorised as impaired loans, regardless of loss expectation.

The provisioning methodology for expired term mortgage loans reflects the latest performance on these accounts.

The Group offers interest only loans to applicants who have credible means to repay the mortgage loan at maturity.

The flow of new interest only residential business has remained low in 2015, representing 2.8% of residential completions. As a result, the proportion of residential interest only mortgages in the portfolio continues to reduce, moving from 24.7% to 19.1% during 2015.

The Group made enhancements to internal monitoring of the interest only portfolio to track closely movements in asset quality and better understand the composition of expired term balances. This management information is regularly reviewed to assess the effectiveness of the Group's interest only policy, contact strategies and to ensure the delivery of fair customer outcomes. Less than 0.1% of the secured portfolio relates to expired term loan balances, with the average balance of these loans around £49,000 and an average LTV of 22%.

Forbearance

	Neither past due nor impaired		Past due not impaired		Impaired		Total	
	£m	%	£m	%	£m	%	£m	%
2015 (audited) **Secured**								
Payment arrangement	3.0	1.2	0.3	3.2	0.3	12.5	3.6	1.4
Transfer to interest only	17.5	7.1	3.3	34.0	0.8	33.3	21.6	8.3
Term extension	171.9	69.5	5.3	54.6	0.7	29.2	177.9	68.6
Payment holiday	55.0	22.2	0.8	8.2	0.6	25.0	56.4	21.7
Total secured forbearance	247.4	100.0	9.7	100.0	2.4	100.0	259.5	100.0
Unsecured								
Accounts where the customer has been approved on a repayment plan	2.9	100.0	–	–	7.8	100.0	10.7	100.0
Total forbearance	250.3	100.0	9.7	100.0	10.2	100.0	270.2	100.0

The value of forbearance stock totalled £270.2 million at 31 December 2015, representing a 3.6% (£10.2 million) reduction on 31 December 2014.

Full Analysis of Risk Classes

	Neither past due nor impaired		Past due not impaired		Impaired		Total	
	£m	%	£m	%	£m	%	£m	%
2014 (audited) **Secured**								
Payment arrangement	2.8	1.1	0.4	2.4	0.1	4.8	3.3	1.2
Transfer to interest only	19.7	7.9	8.6	52.2	0.6	28.6	28.9	10.8
Term extension	162.5	65.3	4.0	24.2	0.9	42.8	167.4	62.6
Payment holiday	63.9	25.7	3.5	21.2	0.5	23.8	67.9	25.4
Total secured forbearance	**248.9**	**100.0**	**16.5**	**100.0**	**2.1**	**100.0**	**267.5**	**100.0**
Unsecured[1]								
Accounts where the customer has been approved on a repayment plan	3.2	100.0	–	–	9.7	100.0	12.9	100.0
Total forbearance	**252.1**	**100.0**	**16.5**	**100.0**	**11.8**	**100.0**	**280.4**	**100.0**

1 The December 2014 forbearance balance was restated to reflect a change in the definition to include customers categorised as in hardship and on a payment plan or vulnerable.

Wholesale credit risk

(audited)	**2015** **£m**	2014 £m
Loans and advances to banks excluding Bank of England	**614.5**	720.5
Bank of England	**888.6**	851.3
Debt securities classified as loans and receivables	**1.1**	8.6
Debt securities classified as available-for-sale financial assets	**1,292.3**	1,539.6
Gross positive fair value of derivative contracts	**82.3**	101.2
Total	**2,878.8**	**3,221.2**

The Group's wholesale credit risk exposures reduced primarily to fund the growth in new loans and advances to customers.

Risk Management Report

Full Analysis of Risk Classes

At 31 December 2015 the single largest exposure to any single counterparty, which is not a sovereign or a supranational obligor, was £130.0 million (2014: £110.1 million). This exposure was to a large counterparty, with a credit rating of A. The table below shows the loans and advances to banks excluding the Bank of England.

(audited)	**2015 £m**	2014 £m
AA+	**16.8**	19.9
AA-	**130.8**	144.4
A+	**205.5**	295.3
A	**174.3**	178.6
A-	**42.1**	39.6
BBB+	**45.0**	42.7
Total	**614.5**	**720.5**

The Group had cash balances with the Bank of England of £888.6 million and £851.3 million as at 31 December 2015 and 2014, respectively. These exposures were rated AA+ at both respective dates.

The table below shows debt securities classified as loans and receivables and debt securities classified as available-for-sale financial assets.

	2015		2014	
(audited)	**Debt securities classified as loans and receivables £m**	**Debt securities classified as available-for-sale financial assets £m**	Debt securities classified as loans and receivables £m	Debt securities classified as available-for-sale financial assets £m
UK sovereign exposures	**–**	**409.5**	–	795.0
Non-domestic sovereign exposures	**–**	**–**	–	–
Supranational	**–**	**203.7**	–	310.7
Residential mortgage-backed securities	**1.1**	**59.4**	8.6	62.9
Covered bonds	**–**	**535.3**	–	265.7
Debt securities issued by banks	**–**	**84.4**	–	105.3
Other	**–**	**–**	–	–
Total	**1.1**	**1,292.3**	**8.6**	**1,539.6**

Full Analysis of Risk Classes

The table below shows the credit rating on debt securities classified as loans and receivables and debt securities classified as available-for-sale financial assets.

(audited)	2015 £m	2014 £m
AAA	**798.4**	508.3
AA+	**434.9**	978.3
AA	**–**	20.9
AA-	**30.0**	–
A+	**29.0**	33.8
A	**1.1**	–
A-	**–**	6.9
Total	**1,293.4**	**1,548.2**

The changes to debt securities reflect a reduction from the high liquidity surplus held at year end 2014. Continued alignment of the Group's liquid asset portfolio to the evolving regulatory definition of high-quality liquid assets is reflected in the decrease in gilt holdings, increase in covered bonds and disposal of unsecured bank debt.

The credit rating of the debt securities remains high, with 95% having a rating of AA+ or better compared to 96% at 31 December 2014.

Derivative financial instruments

The Group reduces exposure to credit risk by using master netting agreements and by obtaining collateral in the form of cash or highly liquid securities. In respect of the Group's maximum credit risk relating to derivative assets of £82.3 million (2014: £101.2 million), cash collateral of £10.6 million (2014: £11.1 million) was held.

The Group measures exposure in over the counter (OTC) derivatives using the gross positive fair value of contracts outstanding with a counterparty, increased by potential future rises in fair value and reduced by gross negative fair value of contracts and collateral received.

While exposures are managed on a net basis, IAS 32 requires that they are represented on the balance sheet on a gross basis. Contracts with positive fair value are disclosed as assets in the balance sheet under 'derivative financial instruments'; those with negative fair value are disclosed as stated on the liabilities side under the same title.

Risk Management Report

Full Analysis of Risk Classes

Collateral received is shown as deposits by banks, with collateral posted shown as loans and advances to banks. The notes to the financial statements provide further information on collateral. The table below details OTC derivative exposures.

(audited)	2015 £m	2014 £m
Gross positive fair value of derivative contracts	**82.3**	101.2
Netting with gross negative fair value of derivative contracts[1]	**(70.4)**	(90.0)
Potential future incremental exposure	**49.9**	49.4
Collateral received	**(10.6)**	(11.1)
Net OTC derivative exposures	**51.2**	**49.5**

1 The use of netting allows positions on all bilateral transactions with any given counterparty to be offset.

The table below provides a summary of net OTC liabilities.

(audited)	2015 £m	2014 £m
Gross negative fair value of derivative contracts	**(151.0)**	(223.1)
Netting with gross positive fair value of derivative contracts[1]	**70.4**	90.0
Collateral pledged (loans and advances to banks)	**76.7**	111.7
Net OTC derivative liability	**(3.9)**	(21.4)

1 The use of netting allows positions on all bilateral transactions with any given counterparty to be offset.

The only netting agreements in place are in relation to derivative financial instruments and repurchase transactions. In respect of repurchase transactions, only the haircut between the asset pledged and deposit received is classed as an exposure given the balance sheet maintains the exposure to the underlying obligor.

The table below provides credit quality analysis of the gross OTC derivative exposures by credit rating of the counterparties.

	2015		2014	
(audited)	£m	%	£m	%
AA-	**22.1**	**26.9**	34.7	34.3
A+	**6.8**	**8.3**	9.6	9.5
A	**42.0**	**51.0**	42.2	41.7
A-	**6.4**	**7.7**	11.2	11.1
BBB+	**5.0**	**6.1**	3.5	3.4
Total	**82.3**	**100.0**	**101.2**	**100.0**

Full Analysis of Risk Classes

Market risk

Definition

Market risk is defined as the risk that the value of, or net income arising from, assets and liabilities changes as a result of interest rate or exchange rate movements. Market risk for the Group arises only as a natural consequence of carrying out and supporting core business activities. The Group does not trade or make markets. As a result interest rate risk is the only material market risk for the Group.

Market risk is assessed across the following classifications: interest rate mismatch risk, basis risk, pipeline risk, optionality risk and foreign currency risk.

Risk appetite

The Group has limited risk appetite for exposures to interest rate risk in the banking book (IRRBB), in terms of both potential changes to economic value, and changes to expected net interest income or earnings. This volatility is managed and reported through a suite of metrics supported by triggers, limits and policies.

Exposures

The Group's banking activities expose it to the risk of adverse movements in interest rates and exchange rates.

Interest rate mismatch risk in the Group's portfolio and in the Group's capital and funding activities arises from the different re-pricing characteristics of the Group's assets, liabilities (see loans and advances to customers on page 160) and off-balance sheet positions of the Group. Interest rate risk arises predominantly from the mismatch between interest rate sensitive assets and liabilities, the variation of volume of business written in response to changes in interest rate, optionality in customers' ability to complete or redeem their products, the investment term of capital and reserves, and the need to stabilise earnings in order to minimise income volatility.

- liabilities are either insensitive to interest rate movements, for example, interest free or very low interest customer deposits, or are sensitive to interest rate changes and bear rates which may be varied at the Group's discretion. There is a significant proportion of deposits with contractually fixed rates for their term to maturity;
- many assets are sensitive to interest rate movements. Some managed rate assets such as variable rate mortgages may be considered as a partial offset to the interest rate risk arising from the managed rate liabilities. A significant proportion of the Group's lending assets (mortgages) bear interest rates which are contractually fixed for periods of up to five years or longer;
- the Group establishes two types of hedge accounting relationships for interest rate risk: fair value hedges and cash flow hedges. The Group is exposed to fair value interest rate risk on fixed rate customer loans, fixed rate customer deposits and to cash flow interest rate risk on variable rate loans and deposits; and
- margin compression risk arises from the current low interest rate environment, which may restrict the ability to change interest rates applied to customers when interbank and central bank rates change.

Basis risk arises from possible changes in spreads, for example, where assets and liabilities reprice at the same time and the scale of rate movement differs.

Pipeline risk arises where new business volumes are higher or lower than forecast, requiring the business to unwind or execute additional hedging at rates which may differ to what was expected.

Optionality risk arises predominantly in retail activities, as customer balances amortise more quickly or slowly than anticipated due to economic conditions or customers' response to changes in economic conditions.

Foreign currency risk arises as a result of having assets, liabilities and derivative items denominated in currencies other than Sterling as a result of banking activities. This includes maintaining liquid assets and wholesale funding. The Group has minimal appetite for foreign currency risk. However, the Group does allow the purchase of liquid assets denominated in both U.S. Dollars and Euros within a well controlled limit framework.

Measurement

The Group uses scenario/stress based risk measures, for example, single factor stresses. These include interest rate re-pricing gaps, earnings sensitivity analysis and open foreign exchange positions.

During May 2015, the European Banking Authority published updated guidelines relating to the management of interest rate risk arising from non-trading activities. The Group expanded

Risk Management Report

Full Analysis of Risk Classes

the IRRBB measurement framework and met regulatory guidelines in advance of the 1 January 2016 application date.

Interest rate risk exposure is monitored as follows:

- Capital at Risk (CaR) is considered for assets and liabilities in all interest rate risk re-pricing periods. This is expressed as the present value of the negative impact of a sensitivity test on the Group's capital position. Risk is measured considering both positive and negative shocks to interest rates. CaR quantifies the change in market value arising from an instantaneous parallel rise or fall in the yield curve, subject to a floor at 0% and relevant non-parallel yield curve stresses. CaR is controlled by a risk appetite limit and supporting metrics; and
- Earnings at Risk (EaR) is considered for assets and liabilities on the forecast balance sheet over a 12 month period. This measure is expressed as the adverse change to net interest income. EaR quantifies the impact to earnings over a rolling 12 month period of an instantaneous parallel rise or fall in the yield curve, subject to a floor at 0%. This measurement is enhanced with non-parallel stress scenarios (basis risk) and behavioural volume stresses (pipeline and optionality). EaR is controlled by a risk appetite limit and supporting metrics.

The Group has an integrated Asset and Liability Management system which allows it to measure and manage interest rate re-pricing profiles (including behavioural assumptions), perform stress testing and produce forecasts.

The following tables show the Group's sensitivities to an instantaneous parallel upward and downward shock to interest rates. The measure is simplified in that it assumes all interest rates for all maturities move at the same time and by the same amount.

Mitigation

As defined within the scope of the Group's IRRBB Policy, the Interest Rate Risk Transfer Pricing framework is used for all hedgeable interest rate risk. Treasury is responsible for managing risk and does this through natural offsets of matching assets and liabilities where possible.

Appropriate hedging activity of residual exposures is undertaken, subject to the authorisation and mandate of the Asset and Liability Committee, within the Board approved risk appetite. Certain residual interest rate risks may remain due to differences in basis and profile mismatches arising from customer behaviour. The impact of this is detailed in the tables on pages 178 and 179.

Monitoring

The Board Risk Committee regularly reviews market risk exposure as part of the wider risk management framework. Levels of exposures are compared to approved limits and triggers.

Capital at Risk

CaR as at 31 December 2015 increased from £26.3 million at 31 December 2014 to £32.2 million in a positive rate shock scenario. The increase in CaR arising under a positive rate shock is primarily due to the growth of fixed rate customer assets and liabilities, where customers may terminate their contract prior to the end of the fixed rate period. The level of CaR under a negative rate shock remains stable.

	2015		2014	
(unaudited)	**Positive rate shock £m**	**Negative rate shock[1] £m**	Positive rate shock £m	Negative rate shock[1] £m
Interest rate mismatch risk	**(3.8)**	**3.1**	(5.7)	4.1
Basis risk	**–**	**–**	0.4	0.4
Pipeline risk	**8.9**	**4.7**	8.1	6.0
Optionality risk	**27.1**	**12.3**	23.5	10.7
Total interest rate risk – capital at risk	**32.2**	**20.1**	**26.3**	**21.2**

1 Market rate (BBR, LIBOR and swaps) stresses are subject to a floor of 0%.

Full Analysis of Risk Classes

Earnings at Risk

EaR as at 31 December 2015 increased from £8.0 million at 31 December 2014 to £15.9 million in a positive rate shock scenario due to an increase in forecast contractually rate insensitive assets which do not reprice in an upward rate shock. EaR in a negative rate shock scenario has decreased by £9.2 million since 2014. The decline reflects revised forecast rate rises throughout the year; as a result, the stress severity reduced.

	2015		2014	
(unaudited)	**Positive rate shock £m**	**Negative rate shock[1] £m**	Positive rate shock £m	Negative rate shock[1] £m
Interest rate mismatch risk	**4.0**	**2.9**	(1.8)	10.9
Basis risk	**(0.2)**	**0.1**	(0.4)	1.1
Pipeline risk	**3.8**	**1.7**	3.7	2.1
Optionality risk	**8.3**	**0.8**	6.5	0.6
Total interest rate risk – earnings at risk	**15.9**	**5.5**	**8.0**	**14.7**

1 Market rate (BBR, LIBOR and swaps) stresses are subject to a floor of 0%.

The Capital and Earnings at Risk measures are based on a parallel stress to the yield curve for interest rate mismatch risk with complementary stress scenarios in other risk categories. The Group recognises that a parallel interest rate stress has inherent limitations and supplements this methodology with additional stress tests and balance sheet limits.

At 31 December 2015 the Group had negligible net foreign exchange risk positions. Potential exposures to changes in exchange rates are minimised by using cross-currency swaps and forward foreign exchange contracts. The table below shows assets and liabilities in foreign currency at sterling carrying values.

	2015		2014	
(audited)	**US$ in £m**	**€ in £m**	US$ in £m	€ in £m
Assets				
Loans and advances to banks	**–**	**–**	–	–
Available-for-sale financial assets	**–**	**3.3**	–	19.4
Other assets	**0.1**	**0.1**	0.1	–
Total assets	**0.1**	**3.4**	0.1	**19.4**
Liabilities				
Other Liabilities	**0.1**	**0.1**	–	–
Total liabilities	**0.1**	**0.1**	–	–
Notional value of derivatives affecting currency exposures	**–**	**–**	–	19.5
Net position	**–**	**3.3**	**0.1**	**(0.1)**

Risk Management Report

Full Analysis of Risk Classes

The following tables give an analysis of the re-pricing periods of assets and liabilities on the balance sheet. Mismatches in the re-pricing timing of assets, liabilities, and off-balance sheet positions create interest rate risk quantified in CaR and EaR.

2015[1] (audited)	Within 3 months £m	After 3 months and within 6 months £m	After 6 months and within 1 year £m	After 1 year and within 5 years £m	After 5 years £m	Non interest bearing instruments £m	Total £m
Assets							
Cash and balances at central banks	835.5	–	–	–	–	53.1	888.6
Loans and receivables:							
Loans and advances to banks	610.0	–	–	–	–	4.5	614.5
Loans and advances to customers	7,201.3	1,710.6	3,132.4	14,407.5	516.9	140.3	27,109.0
Debt securities	1.2	–	–	–	–	(0.1)	1.1
Available-for-sale financial assets	373.2	4.7	59.0	177.9	612.7	69.4	1,296.9
Other assets	–	–	–	–	–	318.9	318.9
Total assets	9,021.2	1,715.3	3,191.4	14,585.4	1,129.6	586.1	30,229.0
Liabilities							
Deposits from banks	1,298.7	–	–	–	–	–	1,298.7
Customer deposits	14,679.4	1,661.6	3,443.6	5,348.6	–	11.7	25,144.9
Debt securities in issue	1,745.9	–	–	300.0	–	(6.5)	2,039.4
Other liabilities	–	–	–	–	–	405.7	405.7
Equity	–	–	–	160.0	–	1,180.3	1,340.3
Total liabilities and equity	17,724.0	1,661.6	3,443.6	5,808.6	–	1,591.2	30,229.0
Notional values of derivatives affecting interest rate sensitivity	7,698.6	199.8	591.2	(7,103.3)	(1,386.3)	–	–
Total interest rate sensitivity gap	(1,004.2)	253.5	339.0	1,673.5	(256.7)	(1,005.1)	–
Cumulative interest rate sensitivity gap	(1,004.2)	(750.7)	(411.7)	1,261.8	1,005.1	–	–

1 Items are allocated to time bands in the table above by reference to the earlier of the next contractual interest rate re-pricing date and the residual maturity date.

Full Analysis of Risk Classes

2014[1] (audited)	Within 3 months £m	After 3 months and within 6 months £m	After 6 months and within 1 year £m	After 1 year and within 5 years £m	After 5 years £m	Non interest bearing instruments £m	Total £m
Assets							
Cash and balances at central banks	803.7	–	–	–	–	47.6	851.3
Loans and receivables:							
Loans and advances to banks	717.4	–	–	–	–	3.1	720.5
Loans and advances to customers	6,842.1	1,247.2	2,522.1	12,004.4	324.1	153.2	23,093.1
Debt securities	11.1	–	–	–	–	(2.5)	8.6
Available-for-sale financial assets	230.1	–	41.7	311.8	841.7	114.3	1,539.6
Other assets	–	–	–	–	–	323.7	323.7
Total assets	**8,604.4**	**1,247.2**	**2,563.8**	**12,316.2**	**1,165.8**	**639.4**	**26,536.8**
Liabilities							
Deposits from banks	846.7	–	–	–	–	–	846.7
Customer deposits	14,381.2	1,108.4	1,827.4	5,025.0	2.0	21.7	22,365.7
Debt securities in issue	1,594.1	–	–	–	–	–	1,594.1
Other liabilities	–	–	–	–	–	486.5	486.5
Equity	–	–	–	160.0	–	1,083.8	1,243.8
Total liabilities and equity	**16,822.0**	**1,108.4**	**1,827.4**	**5,185.0**	**2.0**	**1,592.0**	**26,536.8**
Notional values of derivatives affecting interest rate sensitivity	7,721.4	145.9	(517.7)	(5,799.3)	(1,548.1)	(2.2)	–
Total interest rate sensitivity gap	**(496.2)**	**284.7**	**218.7**	**1,331.9**	**(384.3)**	**(954.8)**	**–**
Cumulative interest rate sensitivity gap	(496.2)	(211.5)	7.2	1,339.1	954.8	–	–

1 Items are allocated to time bands in the table above by reference to the earlier of the next contractual interest rate re-pricing date and the residual maturity date.

The interest rate re-pricing table shown above reflects the re-pricing of assets and liabilities without adjustments to the re-pricing profile that reflect future pricing assumptions or taking into account expected future business that the Group hedges ahead of becoming contractually bound. The Group manages interest rate risk taking these factors into account. Therefore, the increased gap profile shown above does not directly translate to the CaR and EaR term mismatch quantification.

Risk Management Report

Full Analysis of Risk Classes

Operational risk

Definition

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk.

The aim of operational risk management is to manage operational risks in line with defined appetite and to protect both customers and the Group while delivering sustainable growth. The Group's Operational Risk Framework is the method by which operational risks are managed in terms of setting risk appetite, evaluating key exposures, measuring, mitigating, and monitoring risks on an ongoing basis, as set out below.

Risk appetite

The Group's operational risk appetite is designed to safeguard the interests of customers, internal and external stakeholders, and shareholders.

Exposures

The principal operational risks to the Group are:

- IT systems and resilience risk arising from failure to develop, deliver and maintain effective IT solutions;
- information security risk arising from information leakage, loss or theft;
- external fraud arising from an act of deception or omission;
- cyber risk arising from malicious attacks on the Group via technology, networks and systems;
- service disruption;
- failure of a third party corporate partner or strategic supplier; and
- normal business operational risk including transaction processing, information capture and implementation of change.

Measurement

A variety of measures are used such as scoring of potential risks, considering impact and likelihood, assessing the effectiveness of controls, monitoring of events and losses by size, functional area and internal risk categories.

Operational risk exposure and actual losses are used by the Group to calculate the appropriate holding of operational risk capital. The Group calculates Pillar 1 operational risk capital requirements using the Standardised Approach, in line with the Basel Committee guidance.

Mitigation

The Group's control environment is regularly reviewed. Reporting on material risks is discussed monthly by senior management. Risks are managed through a range of strategies – avoidance, mitigation, transfer (including insurance), and acceptance. Contingency plans are maintained for a range of potential scenarios with regular disaster recovery exercises.

Mitigating actions for the principal risks include:

- investment in IT to ensure continued availability, security and resilience of infrastructure;
- investment in information security capability to protect customers and the Group;
- investing in protection of customer information, including access to key systems and the security, durability and accessibility of critical records;
- a risk-based approach to mitigate the financial crime risks the Group faces, reflecting the current and emerging financial crime risks within the market. Through Group-wide policies and operational control frameworks, the Group has developed a comprehensive financial crime operating model. The Group's fraud awareness programme is a key component of the financial crime control environment; and
- operational resilience measures and recovery planning to ensure an appropriate and consistent approach to the management of continuity risks, including potential interruptions from a range of internal and external incidents or threats.

Full Analysis of Risk Classes

Monitoring

Monitoring and reporting of operational risk is undertaken at Board and Executive committees, in accordance with delegated authorities which are regularly reviewed and refreshed. Risk exposure is discussed at the monthly Operational Risk, Conduct Risk and Compliance Committee, and matters are escalated to the Chief Risk Officer, the Risk Management Committee and the Board Risk Committee, where appropriate. A combination of systems, monthly reports, oversight and challenge from the Risk Function, Internal Audit and assurance teams ensures that key risks are regularly presented and debated by executive management.

The Group maintains a formal approach to operational risk event escalation. Material events are identified, captured and escalated. Root causes of events are determined and action plans put in place to ensure an optimum level of control. This ensures the Group keeps customers and the business safe, reduces costs, and improves efficiency.

Key operational risks are appropriately insured and the insurance programme is monitored and reviewed regularly, with recommendations being made to executive management prior to each renewal. Insurers are monitored on an ongoing basis to minimise counterparty risk. A process is in place to manage insurer rating changes.

Risk Management Report

Full Analysis of Risk Classes

Conduct risk and compliance

Definition

Conduct risk and compliance is defined as the risk that the Group's operating model, culture or actions result in unfair outcomes for customers, and the risk of regulatory sanction, material financial loss or reputational damage if the Group fails to design and implement operational processes, systems and controls and maintain compliance with all applicable regulatory requirements.

Risk appetite

The Group has no appetite for regulatory breaches and no tolerance for failing to deliver fair customer outcomes arising from activities, whether through product design, sales or after sales processes. The Group has policies, processes and standards which provide the framework for the business and colleagues to operate in accordance with the laws and regulations which apply to the Group's activities.

Exposures

Conduct risk could affect all aspects of the Group's operations, all types of customers and the Group's stakeholders. The Group faces limited conduct risk in relation to products and services, sales processes and complaint handling.

A series of change programmes drives new legislation and regulation into day-to-day operational and business practices across the Group.

The Group is unburdened with legacy conduct risk issues like PPI, investments or derivatives mis-selling; LIBOR manipulation; or distressed asset portfolios.

Measurement

Risk appetite metrics are regularly reviewed and monitored and include assessments of control and material regulatory rule breaches, complaints and whistleblowing.

Metrics are presented at relevant governance forums for review, challenge and action.

Mitigation

The Group takes a range of mitigating actions with respect to conduct risk and compliance. They include:

- putting the customer at the heart of business planning and strategy;
- using a governance framework that ensures product design and sales processes offer customers value for money, meet the needs of the target market, and deliver fair outcomes to customers, including vulnerable customers;
- using metrics to identify where the Group may be operating outside the risk appetite;
- focusing on recruitment and training and how the Group manages colleagues' performance with clear customer accountabilities;
- creating awareness and providing training to colleagues on the needs of vulnerable customers;
- regulatory horizon scanning;
- using oversight and assurance themed reviews to assess compliance with rules, regulations and policies;
- continuing investment in the Group's IT systems to meet regulatory commitments; and
- escalating material risks and issues to committees that challenge the business on their management.

Full Analysis of Risk Classes

Monitoring

A robust assurance and quality monitoring regime is in place to test the performance of customer critical activities. Customer metrics are proactively used when reviewing business performance and feedback loops have been established to learn from issues identified.

The Risk Function reports on conduct risk and compliance exposure. The report forms the basis of challenge to the business at the monthly Operational Risk, Conduct Risk and Compliance Committee. This committee will escalate matters to the Chief Risk Officer, the Risk Management Committee or the Board Risk Committee, as appropriate.

Risk Management Report

Full Analysis of Risk Classes

Concentration risk[1]

Definition

Concentration risk is defined as the exposure of the Group to credit concentrations in relation to retail and wholesale portfolios, products, obligors and counterparty levels.

Risk appetite

The Group has limited appetite for concentrated exposures by region, loan size, loan type and country.

Concentration risk appetite is reported through a comprehensive suite of metrics.

Exposures

The principal source of concentration risk is from loans and advances to customers in relation to geography, loan size and loan type concentrations in the mortgage portfolio; and from cash, debt securities and derivatives in relation to individual counterparty and country of exposure. The Group has no significant concentrations of risk in the credit card portfolio.

Measurement

Credit concentration risk is measured through the application of limits relating to each concentration category.

1 All risk class components of financial risk are outlined on page 149. Concentration risk is the most significant component of financial risk and therefore has been disclosed in detail.

Mitigation

Credit risk management includes portfolio controls on product lines and risk segments to reflect risk appetite and individual limit guidelines. Credit policy is aligned to the Group's risk appetite and restricts exposure to more vulnerable sectors and segments. Exposures are monitored to prevent an excessive concentration of risk. The Group's larger exposures are reported in accordance with regulatory reporting requirements.

Monitoring

Monthly reporting on concentration risk exposures is made to the Board.

Secured credit

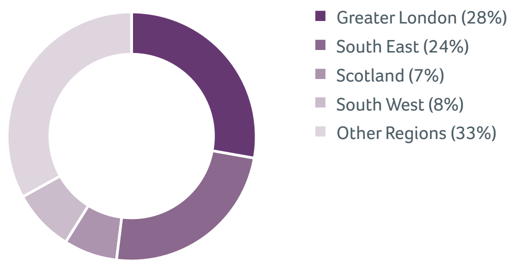
There has been significant focus on house price inflation since the end of 2013 with London and the South East experiencing significantly higher levels of house price growth than the rest of the UK. Whilst demand for London property may be influenced by the international market, concerns over an asset bubble forming in these two regions are based on the rate of growth relative to other regions, a potential divergence in supply and demand for property, and customer affordability being stretched. The Group's policy broadly restricts LTV for higher value loans, resulting in the lower average new lending LTVs observed in London (63%) and the South East (68%) compared to other regions (72%). The Group made changes to its lending policy in 2014 in response to this risk by introducing income multiple and higher debt-to-income ratios caps for all residential mortgages loans. While the policy is applied at a national level, it predominantly affects London and the South East.

Full Analysis of Risk Classes

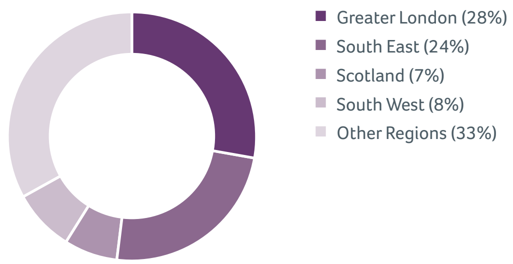
The table below shows the geographical concentration of the mortgage portfolio.

	2015		2014	
(audited)	£m	%	£m	%
East Anglia	**605.9**	**2.5**	517.8	2.4
East Midlands	**1,287.8**	**5.1**	1,071.6	4.9
North	**957.0**	**3.8**	919.2	4.2
Yorkshire & Humberside	**1,413.0**	**5.5**	1,232.0	5.6
North West	**1,890.7**	**7.4**	1,652.1	7.5
West Midlands	**1,302.3**	**5.1**	1,078.2	4.9
South West	**1,936.2**	**7.6**	1,696.3	7.7
South East	**6,139.4**	**24.1**	5,178.8	23.7
Greater London	**7,230.0**	**28.4**	6,037.0	27.6
Wales	**597.4**	**2.3**	547.0	2.5
Scotland	**1,685.5**	**6.6**	1,616.3	7.4
Northern Ireland	**416.5**	**1.6**	347.9	1.6
Other	**0.5**	**–**	0.9	–
Total	**25,462.2**	**100.0**	**21,895.1**	**100.0**

2015



2014



The geographical split of the portfolio remains broadly stable.

Risk Management Report

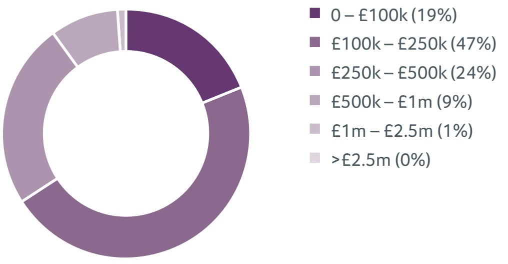
Full Analysis of Risk Classes

The table below shows retail secured credit concentrations by loan size.

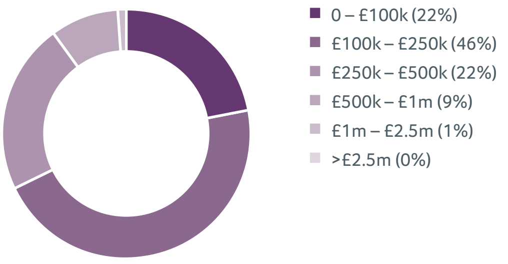
	2015		2014	
(audited)	**£m**	**%**	£m	%
0-£100k	**4,941.5**	**19.4**	4,722.5	21.5
£100k-£250k	**11,878.2**	**46.6**	10,023.9	45.8
£250k-£500k	**6,078.0**	**23.9**	4,851.3	22.2
£500k-£1m	**2,334.3**	**9.2**	2,068.1	9.4
£1m-£2.5m	**211.3**	**0.8**	210.1	1.0
>£2.5m	**18.9**	**0.1**	19.2	0.1
Total	**25,462.2**	**100.0**	**21,895.1**	**100.0**

As at 31 December 2015, 0.9% (2014: 1.1%) of mortgage balances consisted of loans in excess of £1 million.

2015



2014



The proportion of loans with balances of up to £250,000 increased by £2.1 billion in 2015. This represents 58% of the total secured loans portfolio growth of £3.6 billion.

The table below shows retail secured credit average LTV by loan size.

2015 (audited)	**Residential mortgage Loans %**	**Residential buy-to-let mortgage loans %**	**Total**
0-£100k	**42.9**	**57.9**	**47.9**
£100k-£250k	**58.9**	**56.5**	**58.5**
£250k-£500k	**56.5**	**49.5**	**55.9**
£500k-£1m	**51.6**	**43.9**	**51.0**
£1m-£2.5m	**46.5**	**35.9**	**44.9**
>£2.5m	**43.8**	**–**	**43.8**
Total	**54.9**	**55.4**	**55.0**

Full Analysis of Risk Classes

2014 (audited)	Residential mortgage Loans %	Residential buy-to-let mortgage loans %	Total
0-£100k	45.0	57.8	48.4
£100k-£250k	59.9	56.3	59.5
£250k-£500k	57.2	51.3	56.7
£500k-£1m	53.4	46.1	52.9
£1m-£2.5m	50.8	40.3	49.1
>£2.5m	44.8	–	44.8
Total	**55.8**	**55.6**	**55.7**

The Group's policy broadly restricts LTV for higher value loans. The average LTV for each loan band demonstrates that, excluding loans under £100,000, higher value loans have lower LTVs. The average indexed LTV across the loan size bands has decreased reflecting continued house price growth in 2015.

Page 153 details policy changes for income multiples and higher debt to income levels. These were designed to improve the resilience of the portfolio to any reversal of house price inflation gains that were seen since 2014, or future interest rate rises.

Loan type

The residential mortgage loan portfolio comprises three principal loan repayment types:

- capital repayment loans amortise monthly through customer repayments which comprise an interest payment and contribution to the principal loan balance;
- part and part loans provide customers with the flexibility to choose to pay a proportion of the loan on a capital repayment basis and a proportion on interest only, with the interest only element repaid from an acceptable repayment vehicle; and
- interest only loans allow borrowers to pay only the interest on the loan each month, with the capital to be repaid in full at the end of the loan period from an acceptable repayment vehicle. For residential mortgage customers, the Group continues to apply strict affordability criteria and restricts applicant loan-to-value. For buy-to-let customers, interest only mortgages continue to be the predominant repayment method, with the majority of customers looking to the sale of the mortgaged property as the ultimate loan repayment vehicle. These loans are also subject to stringent lending standards.

The tables below show retail secured credit concentrations by loan type.

	Residential mortgage loans		**Residential buy-to-let mortgage loans**		**Total**	
	£m	**%**	**£m**	**%**	**£m**	**%**
2015 (audited)						
Capital repayment	**15,800.7**	**75.0**	**761.0**	**17.3**	**16,561.7**	**65.0**
Part and part	**1,235.4**	**5.9**	**26.5**	**0.6**	**1,261.9**	**5.0**
Interest only	**4,024.2**	**19.1**	**3,614.4**	**82.1**	**7,638.6**	**30.0**
Total	**21,060.3**	**100.0**	**4,401.9**	**100.0**	**25,462.2**	**100.0**

Risk Management Report

Full Analysis of Risk Classes

	Residential mortgage loans		Residential buy-to-let mortgage loans		Total	
	£m	%	£m	%	£m	%
2014 (audited)						
Capital repayment	12,712.5	67.7	556.9	17.8	13,269.4	60.6
Part and part	1,419.9	7.6	23.9	0.8	1,443.8	6.6
Interest only	4,627.1	24.7	2,554.8	81.4	7,181.9	32.8
Total	**18,759.5**	**100.0**	**3,135.6**	**100.0**	**21,895.1**	**100.0**

Interest only residential new lending has remained low at 2.8% of total residential mortgage completions for 2015. As a result, the proportion of residential interest only loans has decreased from 24.7% to 19.1%.

Wholesale

Concentration risk is managed for both individual counterparties and for country of exposure. The Group does not set a limit to exposures to the Bank of England and the UK Sovereign. The table below shows exposures by country.

(audited)	**2015 £m**	2014 £m
Australia	**63.2**	88.3
Canada	**108.9**	151.1
France	**67.7**	84.0
UK	**2,234.9**	2,373.7
Germany	**10.9**	6.6
Netherlands	**73.8**	118.8
Norway	**24.0**	44.8
Sweden	**20.0**	–
USA	**71.7**	43.2
Supranational	**203.7**	310.7
Total	**2,878.8**	**3,221.2**

The Group's wholesale credit risk exposures reduced primarily to fund the growth in new loans and advances to customers.

The Group's wholesale credit risk exposure outside the UK remains well diversified.

Full Analysis of Risk Classes

Funding and liquidity risk

Definition

Funding risk is defined as the inability to raise and maintain sufficient funding in quality and quantity to support the delivery of the business plan. Sound funding risk management reduces the likelihood of liquidity risks occurring through minimising refinancing concentration.

Liquidity risk is defined as the inability to accommodate liability maturities and withdrawals, fund asset growth and otherwise meet contractual obligations to make payments as they fall due.

Risk appetite

The Group has an appetite to maintain sufficient liquidity resources which are adequate, in both amount and quality, to ensure that it is able to meet its financial obligations and regulatory requirements. Balance sheet limits and metrics shape the funding strategy to ensure growth is delivered through stable and sustainable sources, managing refinancing, tenor and concentration risks.

Exposures

Liquidity exposure represents the amount of potential stressed outflows in any future period less expected inflows. Liquidity is considered from both an internal and a regulatory perspective.

Measurement

A series of measures is used across the Group to monitor both short and long-term liquidity including ratios, cash outflow triggers, wholesale and retail funding maturity profile, early warning indicators and stress test survival period triggers. Liquidity risk appetite covers a range of metrics considered key to maintaining a strong liquidity and funding position and is regularly reported to the Board Risk Committee and the Board. Strict criteria and limits are in place to ensure highly liquid marketable securities are available as part of the portfolio of liquid assets.

Details of contractual maturities for assets and liabilities form an important source of information for the management of liquidity risk.

In order to reflect more accurately the expected behaviour of the Group's assets and liabilities, measurement and modelling of the behavioural aspects of each is calculated.

Mitigation

The Group mitigates the risk of a liquidity mismatch in excess of risk appetite by managing the liquidity profile of the balance sheet through short-term liquidity management and over the life of the funding plan. Short-term liquidity management is considered from two perspectives: business as usual and liquidity under stressed conditions, both of which relate to funding within one year. The Group measures risk appetite and liquidity position as the quantum of liquid assets available in excess of the minimum requirements set by total stress outflows.

Longer term funding is used to manage the Group's strategic liquidity profile which is determined by the Group's balance sheet structure. Longer term is defined as having an original maturity of more than one year.

The most material component of the Group's funding and liquidity position is the customer deposit base, and is supplemented by wholesale funding providing a source of stable funding for balance sheet growth. A substantial proportion of the retail deposit base is made up of customers' savings accounts which, although mostly repayable on demand, have traditionally provided a stable source of funding. Funding concentration by counterparty is not considered significant for the Group. Where concentrations do exist for example, refinancing at maturity, these are managed within the appropriate internal risk appetite.

The Group operates a Funds Transfer Pricing (FTP) mechanism which:

- drives customer pricing and supports the overall Group balance sheet strategy; and
- is consistent with regulatory requirements.

FTP makes use of behavioural maturity profiles, taking account of expected customer loan prepayments and the stability of customer deposits. Such behavioural maturity assumptions are subject to formal governance and reviewed periodically.

The ability to deploy assets quickly, either through the repo market or through outright sale, is also an important source of liquidity for the Group. In addition to central bank reserves, the Group holds sizeable balances of high-quality marketable debt securities which can be sold to provide, or used to secure, additional cash inflows should the need arise from either market counterparties or central bank facilities (Bank of England).

Risk Management Report

Full Analysis of Risk Classes

Monitoring

Liquidity is actively monitored by the Treasury and Risk Functions. Reporting is conducted through the Group's committee structure, in particular the Asset and Liability Committee and the Board Risk Committee. In a stress situation the level of monitoring and reporting is increased commensurate with the nature of the stress event. Liquidity policies and procedures are subject to independent internal oversight.

Daily monitoring and control processes are in place to address internal and regulatory liquidity requirements. The Group monitors a range of market and internal early warning indicators on a daily basis for early signs of liquidity risk in the market or specific to the Group. These are a mixture of quantitative and qualitative measures including daily variation of customer balances, cash outflows, changes in primary liquidity portfolio, credit default swap spreads and changing funding costs.

In addition, the monitoring framework has two other important components:

- firstly, the volume and quality of the Group's liquid asset portfolio is defined through a series of stress tests across a range of time horizons and stress conditions. The Group ensures a liquidity surplus is held during normal market conditions above liquidity stress outflow requirements. Stress cash outflow assumptions have been established for individual liquidity risk drivers across idiosyncratic and market wide stresses.

  Internal and regulatory liquidity requirements are quantified on a daily basis, with holdings assessed against a full suite of liquidity stresses weekly.

  As at 31 December 2015, the results of stress testing of liquidity outflows were £3.1 billion (2014: £2.8 billion). This is significantly below the level of liquidity held by the Group. Risk drivers of this liquidity stress outflow are detailed in the following table. The Group is predominantly retail funded. As a result the largest potential source of liquidity stress is the outflow of retail customer deposits.

  The key risk driver assumptions applied to the scenarios are:

Liquidity risk driver	Modelling assumption
Retail funding	Severe unexpected withdrawals of retail deposits, the scale of which is based on the experience during the financial crisis with adjustments taking into account changes in depositor protection, the Group's liability profile and customer behaviour. No additional deposit inflows are assumed.
Wholesale funding	Limited opportunity to refinance wholesale contractual maturities with the exception of repo funding by the Bank of England or market participants using central bank eligible collateral.
Off-balance sheet	Cash outflows continue as a result of off-balance sheet commitments such as mortgage pipeline, undrawn credit card facilities and collateral commitments.
Marketable asset risk	Assets held for liquidity purposes experience deterioration in market availability and resulting value.

  The scenarios and the assumptions are reviewed at least annually to ensure that they continue to be relevant to the nature of the business. The Group's liquidity risk appetite is calibrated against a number of stressed metrics. The funding plan is also stressed against a range of macroeconomic scenarios; and

- secondly, the Group maintains a Contingency Funding Plan which is designed to provide an early warning indicator for liquidity concerns. As a result, mitigating actions can be taken to avoid a more serious situation developing. Contingency Funding Plan invocation and escalation processes are based on analysis of five major quantitative and qualitative components. They comprise an assessment of early warning indicators, prudential and regulatory liquidity risk limits and triggers, stress testing results, event and systemic indicators and market intelligence.

  The introduction of the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio as part of CRD IV are intended to raise the resilience of banks to potential liquidity shocks and provide the basis for a harmonised approach to liquidity risk management. The LCR became the Pillar 1 standard for liquidity in the UK from 1 October 2015. As at 31 December, the Group had an LCR of 202.1% based on the PRA's guidance for calculation. The Group manages LCR within an internal risk limit above the European and UK regulatory requirements.

Full Analysis of Risk Classes

Funding and liquidity management in 2015

The Group is predominantly funded through customer deposits. During 2015, the Group maintained a strong presence in the retail savings market, increasing total customer deposits by £2,779 million. The focus of retail funding was fixed rate ISAs, growing 68.9% since December 2014.

Wholesale funding is used to support balance sheet growth, lengthen the tenor of funding and diversify sources of funding. The Group has continued to diversify its sources of wholesale funding, issuing an inaugural Medium Term Note, raising funds through the well-established Residential Mortgage Backed Securities (RMBS) Gosforth programme and through additional drawings from the BoE Funding for Lending Scheme (FLS) facility. The volume of Term Repo has increased by £440 million through the use of repurchase agreements to fund lending growth. The volume of encumbered assets has increased as a result of additional FLS, Term Repo and RMBS issuance.

Group funding sources

The Group's loan-to-deposit ratio has increased to 107.5% compared with 102.8% at 31 December 2014, driven by increased retail lending activities supported by growth in secured wholesale funding and a reduction in surplus liquidity. The table below shows funding position.

(audited)	**2015 £m**	2014 £m
Loans and advances to customers	**27,109.0**	23,093.1
Loans and advances to banks	**614.5**	720.5
Debt securities classified as loans and receivables	**1.1**	8.6
Available-for-sale financial assets (encumbered)	**–**	321.7
Cash and balances at central banks (encumbered)	**160.5**	38.0
Funded assets	**27,885.1**	24,181.9
Other assets	**318.9**	323.7
Total assets (excluding liquid assets)	**28,204.0**	24,505.6
On balance sheet primary liquidity assets		
Cash and balances at central banks – primary	**728.1**	813.3
Available-for-sale financial assets (unencumbered)	**1,296.9**	1,217.9
Total assets	**30,299.0**	26,536.8
Less: Other liabilities	**(429.5)**	(497.9)
Funding requirement	**29,799.5**	26,038.9
Funded by		
Customer deposits	**25,144.9**	22,365.7
Wholesale funding	**3,314.3**	2,429.4
Total equity	**1,340.3**	1,243.8
Total funding	**29,799.5**	**26,038.9**

Risk Management Report

Full Analysis of Risk Classes

Asset origination was funded partly by an increase in wholesale funding. The table below shows the sources of wholesale funding.

(audited)	**2015 £m**	2014 £m
Debt securities in issue	**2,039.4**	1,594.1
Term repo	**1,274.9**	835.3
Total on-balance sheet sources of funds	**3,314.3**	2,429.4
FLS drawings	**2,960.0**	2,260.0
Total	**6,274.3**	**4,689.4**

The tables below show residual maturity of the wholesale funding book.

2015 (audited)	**Within 3 months £m**	**3-12 months £m**	**1-5 years £m**	**After 5 years £m**	**Total £m**
Debt securities in issue	**–**	**–**	**297.5**	**1,741.9**	**2,039.4**
Term repo	**749.9**	**525.0**	**–**	**–**	**1,274.9**
Total on-balance sheet sources of funds	**749.9**	**525.0**	**297.5**	**1,741.9**	**3,314.3**
FLS drawings	**–**	**510.0**	**2,450.0**	**–**	**2,960.0**
Total	**749.9**	**1,035.0**	**2,747.5**	**1,741.9**	**6,274.3**

2014 (audited)	Within 3 months £m	3-12 months £m	1-5 years £m	After 5 years £m	Total £m
Debt securities in issue	–	–	–	1,594.1	1,594.1
Term repo	272.3	563.0	–	–	835.3
Total on-balance sheet sources of funds	272.3	563.0	–	1,594.1	2,429.4
FLS drawings	–	–	2,260.0	–	2,260.0
Total	**272.3**	**563.0**	**2,260.0**	**1,594.1**	**4,689.4**

The increase in FLS drawings is offset by the continued pay down of the Gosforth RMBS programme, leaving the average tenor of wholesale funding stable.

Full Analysis of Risk Classes

Encumbered assets

The Group's assets can be used to support funding collateral requirements for central bank operations or third party re-purchase transactions. Assets that have been set aside for such purposes are classified as 'encumbered and pledged assets' and cannot be used for other purposes. The tables below show asset encumbrance.

	Encumbered assets		Unencumbered assets		
2015 (audited)	Pledged as collateral £m	Other[1] £m	Available as collateral[2] £m	Other[3] £m	Total £m
Cash and balances at central banks[4]	160.5	–	–	728.1	888.6
Debt securities classified as loans and receivables	–	–	1.1	–	1.1
Available-for-sale financial assets	–	–	1,292.3	4.6	1,296.9
Derivative financial assets	–	–	–	82.3	82.3
Loans and advances to banks	–	478.6	–	135.9	614.5
Loans and advances to customers[5]	7,524.1	–	3,153.5	16,431.4	27,109.0
Other assets	–	–	–	236.6	236.6
Total Assets	**7,684.6**	**478.6**	**4,446.9**	**17,618.9**	**30,229.0**
Treasury bills raised through FLS held off balance sheet[6]	786.0	–	2,174.0	–	2,960.0
Total Assets plus off balance sheet FLS	**8,470.6**	**478.6**	**6,620.9**	**17,618.9**	**33,189.0**

1 Other encumbered assets are assets that cannot be used for secured funding due to legal or other reasons. These include cash reserves supporting secured funding structures.

2 Unencumbered assets which are classified as 'available as collateral' are readily available to secure funding or to meet collateral requirements. Loans and advances to customers are classified as 'available as collateral' only if they are already in such a form that they can be used immediately to raise funding.

3 Other unencumbered assets are assets which are not subject to any restrictions and are not readily available for use.

4 Encumbered cash and balances at central banks includes the minimum reserve collaterisation requirement for the BACS payment system, introduced in September 2015.

5 Loans and advances to customers consist of collateral pledged to the Bank of England and securitised mortgage pools.

6 These include Treasury Bills received by the Group through FLS which are not recognised on the balance sheet. These are classified as unencumbered when the Group is permitted to re-pledge.

Risk Management Report

Full Analysis of Risk Classes

2014 (audited)	Encumbered assets: Pledged as collateral £m	Encumbered assets: Other[1] £m	Unencumbered assets: Available as collateral[2] £m	Unencumbered assets: Other[3] £m	Total £m
Cash and balances at central banks[4]	38.0	–	–	813.3	851.3
Debt securities classified as loans and receivables	–	–	8.6	–	8.6
Available-for-sale financial assets	321.7	–	1,217.9	–	1,539.6
Derivative financial assets	–	–	–	101.2	101.2
Loans and advances to banks	–	569.8	–	150.7	720.5
Loans and advances to customers[5]	6,609.4	–	2,075.0	14,408.7	23,093.1
Other assets	–	–	–	222.5	222.5
Total Assets	**6,969.1**	**569.8**	**3,301.5**	**15,696.4**	**26,536.8**
Treasury bills raised through FLS held off balance sheet[6]	–	–	2,260.0	–	2,260.0
Total Assets plus off balance sheet FLS	**6,969.1**	**569.8**	**5,561.5**	**15,696.4**	**28,796.8**

1 Other encumbered assets are assets that cannot be used for secured funding due to legal or other reasons. These include cash reserves supporting secured funding structures.

2 Unencumbered assets which are classified as 'available as collateral' are readily available to secure funding or to meet collateral requirements. Loans and advances to customers are classified as 'available as collateral' only if they are already in such a form that they can be used immediately to raise funding.

3 Other unencumbered assets are assets which are not subject to any restrictions and are not readily available for use.

4 Encumbered cash and balances at central banks includes the minimum reserve collaterisation requirement for the BACS payment system, introduced in September 2015.

5 Loans and advances to customers consist of collateral pledged to the Bank of England and securitised mortgage pools.

6 These include Treasury Bills received by the Group through FLS which are not recognised on the balance sheet. These are classified as unencumbered when the Group is permitted to re-pledge.

The Group's total level of asset encumbrance increased to 27.0% compared with 26.2% at 31 December 2014. Encumbrance of assets predominantly arises from the use of the BoE FLS liquidity facility and from the Gosforth RMBS programme. The Group manages the volume of available unencumbered collateral to meet requirements arising from current and future secured funding transactions. During 2015, the Group's unencumbered loans and advances to customers increased by £3,101 million as a result of using wholesale funding to support increased lending.

Full Analysis of Risk Classes

The Group maintains a portfolio of liquid assets in accordance with risk appetite. Liquid assets are held predominantly in high-quality unencumbered securities issued by the UK Government or supranationals and deposits with central banks. The portfolio mix is aligned to the liquidity coverage requirement defined in European liquidity regulatory standards. Other liquidity resources represent additional unencumbered liquid assets held over and above high-quality liquid assets. These are intended to cover more extreme stress events and provide flexibility for liquidity management. The table below shows composition of the liquidity portfolio.

(unaudited) **Level 1**	**2015** **£m**	**2015** **Average** **£m**	2014 £m	2014 Average £m
Cash and balances at central banks	**846.3**	**796.4**	813.3	1,120.9
UK Government securities	**409.5**	**392.6**	586.2	637.8
Other HQLA level 1 eligible	**25.4**	**15.8**	–	33.9
Supranational securities	**203.7**	**294.6**	310.7	350.1
Treasury bills raised through FLS	**2,174.0**	**2,150.6**	2,260.0	1,598.5
Covered bonds (Level 1 eligible)[1]	**498.2**	**248.2**	–	–
Total level 1	**4,157.1**	**3,898.2**	**3,970.2**	**3,741.2**
Level 2a				
Covered bonds (Level 2a eligible)[1]	**22.1**	**133.5**	225.7	127.9
Total level 2a	**22.1**	**133.5**	**225.7**	**127.9**
Level 2b				
Eligible RMBS	**59.4**	**44.7**	40.0	42.1
Total level 2b	**59.4**	**44.7**	**40.0**	**42.1**
High quality liquid assets (Level 1 + 2a + 2b)	**4,238.6**	**4,076.4**	4,235.9	3,911.2
Other liquidity resources				
Covered bonds	**15.0**	**2.3**	–	–
Non-eligible RMBS	**–**	**3.0**	8.6	8.8
Certificates of deposit	**59.0**	**4.5**	–	43.8
Floating rate notes	**–**	**–**	–	11.1
Fixed rate bonds	**–**	**17.0**	55.3	120.3
Money market loans	**54.0**	**30.9**	–	–
Total other liquidity resources	**128.0**	**57.7**	**63.9**	**184.0**
Self-issued RMBS	**326.7**	**197.6**	92.8	433.4
Total liquidity	**4,693.3**	**4,331.7**	**4,392.6**	**4,528.6**

1 During 2015, the Group reclassified covered bonds to align with the European Commission's delegated act with regard to the liquidity coverage requirement. The legislation prescribes a liquidity classification based on several criteria, including the credit quality and indicators of liquidity performance under stress conditions of the instrument.

The Group holds sufficient liquidity to meet all internal and regulatory liquidity requirements.

Risk Management Report

Full Analysis of Risk Classes

The tables below analyse assets and liabilities of the Group into relevant maturity groupings based on the remaining contractual period at the balance sheet date. The Group's assets and liabilities may be repaid or otherwise mature earlier or later than implied by their contractual terms, and readers are therefore advised to use caution when using this data to evaluate the Group's liquidity position. In particular, amounts in respect of customer deposits are usually contractually payable on demand or at short notice. In practice, these deposits are not usually withdrawn on their contractual maturity.

2015 (audited) **Assets**	**Within 3 months £m**	**3-12 months £m**	**1-5 years £m**	**After 5 years £m**	**Total £m**
Cash and balances at central banks	846.9	–	–	41.7	888.6
Derivative financial instruments	16.1	13.3	47.4	5.5	82.3
Loans and receivables:					
Loans and advances to banks	614.5	–	–	–	614.5
Loans and advances to customers	1,778.0	572.5	3,334.6	21,423.9	27,109.0
Debt securities	–	–	–	1.1	1.1
Available-for-sale financial assets	47.5	4.7	424.4	820.3	1,296.9
Other assets	47.5	20.2	14.8	154.1	236.6
Total assets	3,350.5	610.7	3,821.2	22,446.6	30,229.0
Liabilities					
Deposits from banks	773.7	525.0	–	–	1,298.7
Customer deposits	20,776.5	2,630.2	1,738.2	–	25,144.9
Derivative financial instruments	5.9	12.1	103.2	34.8	156.0
Debt securities in issue	–	–	297.5	1,741.9	2,039.4
Other liabilities	158.8	46.9	39.5	4.5	249.7
Total liabilities	21,714.9	3,214.2	2,178.4	1,781.2	28,888.7
Net liquidity (gap)/surplus	(18,364.4)	(2,603.5)	1,642.8	20,665.4	1,340.3

Full Analysis of Risk Classes

2014 (audited) **Assets**	Within 3 months £m	3-12 months £m	1-5 years £m	After 5 years £m	Total £m
Cash and balances at central banks	813.3	–	–	38.0	851.3
Derivative financial instruments	6.7	12.8	70.7	11.0	101.2
Loans and receivables:					
Loans and advances to banks	720.5	–	–	–	720.5
Loans and advances to customers	1,264.8	468.6	2,859.7	18,500.0	23,093.1
Debt securities	–	–	–	8.6	8.6
Available-for-sale financial assets	20.1	122.2	406.0	991.3	1,539.6
Other assets	41.2	28.1	34.6	118.6	222.5
Total assets	**2,866.6**	**631.7**	**3,371.0**	**19,667.5**	**26,536.8**
Liabilities					
Deposits from banks	283.7	563.0	–	–	846.7
Customer deposits	18,041.0	2,356.4	1,967.4	0.9	22,365.7
Derivative financial instruments	6.3	6.8	133.1	82.0	228.2
Debt securities in issue	–	–	–	1,594.1	1,594.1
Other liabilities	191.7	42.5	19.3	4.8	258.3
Total liabilities	**18,522.7**	**2,968.7**	**2,119.8**	**1,681.8**	**25,293.0**
Net liquidity (gap)/surplus	(15,656.1)	(2,337.0)	1,251.2	17,985.7	1,243.8

Risk Management Report

Full Analysis of Risk Classes

Cashflow profile

The table below divides the Group's non-derivative cash outflows into relevant maturity groupings based on the remaining period between the balance sheet date and the contractual maturity date. The amounts disclosed are the contractual undiscounted cash flows. These differ from balance sheet values due to the effects of discounting on certain balance sheet items and due to the inclusion of contractual future interest flows.

2015 (audited)	**Within 3 months £m**	**3-6 months £m**	**6-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Total £m**
Deposits from banks	**775.8**	**526.3**	**–**	**–**	**–**	**1,302.1**
Customer deposits	**21,228.6**	**895.0**	**1,604.4**	**1,962.0**	**–**	**25,690.0**
Debt securities in issue	**152.3**	**236.7**	**208.3**	**1,550.4**	**–**	**2,147.7**
Total	**22,156.7**	**1,658.0**	**1,812.7**	**3,512.4**	**–**	**29,139.8**

2014 (audited)	Within 3 months £m	3-6 months £m	6-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Deposits from banks	284.4	564.9	–	–	–	849.3
Customer deposits	18,151.5	1,372.4	1,140.9	2,204.6	1.0	22,870.4
Debt securities in issue	185.3	128.7	223.5	1,123.4	–	1,660.9
Total	**18,621.2**	**2,066.0**	**1,364.4**	**3,328.0**	**1.0**	**25,380.6**

Fixed rate ISAs have been the main source of retail funding throughout 2015. As the table reflects deposits on a contractual basis, these are disclosed in the 'within 3 months' category, resulting in a shortening of the Group's contractual cashflow profile of customer deposits.

The tables below divide the undiscounted derivative cash outflows into relevant maturity groupings based on the remaining period between the balance sheet date and the contractual maturity date. Cash flows for the floating legs of derivative transactions are calculated based on market indications of future interest rates. As a result, totals in these tables are not intended to be identical to tables on OTC derivatives or the notes to the financial statements by definition.

2015 (audited) **Settled on a net basis**	**Within 3 months £m**	**3-6 months £m**	**6-12 months £m**	**1-5 years £m**	**Over 5 years £m**	**Total £m**
Derivatives in economic and not accounting hedges	**(1.1)**	**0.2**	**(0.6)**	**(13.5)**	**(0.9)**	**(15.9)**
Derivatives in accounting hedge relationships	**(30.9)**	**(25.1)**	**(35.8)**	**(41.6)**	**(3.2)**	**(136.6)**
	(32.0)	**(24.9)**	**(36.4)**	**(55.1)**	**(4.1)**	**(152.5)**
Settled on a gross basis						
Outflows	**–**	**–**	**–**	**–**	**–**	**–**
Inflows	**–**	**–**	**–**	**–**	**–**	**–**
Derivatives in accounting hedge relationships	**–**	**–**	**–**	**–**	**–**	**–**
Total	**(32.0)**	**(24.9)**	**(36.4)**	**(55.1)**	**(4.1)**	**(152.5)**

Full Analysis of Risk Classes

2014 (audited) **Settled on a net basis**	Within 3 months £m	3-6 months £m	6-12 months £m	1-5 years £m	Over 5 years £m	Total £m
Derivatives in economic and not accounting hedges	(2.8)	(2.2)	(5.5)	(9.4)	(2.5)	(22.4)
Derivatives in accounting hedge relationships	(31.6)	(22.9)	(45.8)	(91.2)	(12.6)	(204.1)
	(34.4)	(25.1)	(51.3)	(100.6)	(15.1)	(226.5)
Settled on a gross basis						
Outflows	–	–	–	–	–	–
Inflows	–	–	–	–	–	–
Derivatives in accounting hedge relationships	–	–	–	–	–	–
Total	**(34.4)**	**(25.1)**	**(51.3)**	**(100.6)**	**(15.1)**	**(226.5)**

External credit ratings

Virgin Money Holdings (UK) plc does not have an external credit rating. Disclosures below relate to its subsidiary, Virgin Money plc. Virgin Money plc's short and long-term credit ratings as at 31 December 2015 are as follows.

	Long term	Short term	Outlook	Date of last rating action	Rating action type
Fitch	BBB+	F2	Positive	19 November 2015	Affirmed

In November 2015 the rating agency Fitch revised Virgin Money plc's outlook to Positive from Stable and affirmed its long-term rating at BBB+.

The table below sets out the amount of additional collateral the Company would need to provide in the event of a one and two notch downgrade by external credit ratings agencies.

	Cumulative adjustment for a one-notch downgrade £m	Cumulative adjustment for a two-notch downgrade £m
2015	**–**	**10.0**
2014	–	10.0

Risk Management Report

Full Analysis of Risk Classes

Capital

Definition

Capital risk is defined as the risk that the Group has a sub-optimal amount or quality of capital or that capital is inefficiently deployed across the Group.

Risk appetite

Board strategic planning is based on clear principles which aim to ensure that an appropriate balance of risk and reward is achieved in growing a sustainable business. This is reflected in a clearly defined risk appetite for capital which aids the Group in maintaining a high-quality capital base, targeting capital ratios which support business development and are in excess of regulatory minimum.

Capital resources

A capital shortfall arises where the Group has insufficient capital resources to support the strategic objectives and plans. The Group's capital management approach is focused on maintaining sufficient capital resources to prevent such exposures while optimising value for shareholders.

Measurement of capital

The Group calculates capital resources and requirements using the CRD IV CRR regulatory framework as implemented by the PRA. Pillar 1 capital requirements are calculated in respect of credit risk, operational risk, market risk and credit valuation adjustments. The capital requirement for residential mortgages is measured using an Advanced Internal Ratings Based (AIRB) approach approved by the PRA, and all other requirements are calculated using the Standardised Approach.

The Group uses AIRB models in measuring the credit risk of secured loans and advances to customers. They reflect three components: (i) the 'probability of default' by the borrowers on their contractual obligations, (ii) current exposures to the borrowers and their likely future development, from which the Group derives the 'exposure at default', and (iii) the likely loss ratio on the defaulted obligations (the 'loss given default'). These parameters are used in order to derive an expected loss. In contrast, impairment allowances are recognised for financial reporting purposes only for loss events that have occurred at the balance sheet date, based on objective evidence of impairment.

Due to the different methodologies applied, the amount of incurred credit loss provisions in the financial statements differs from the amount determined from expected loss models used for internal operational management, capital requirement and other banking regulation purposes. Page 161 provides details of the Group's approach to the impairment of financial assets. Further details can also be found in note 1 to the financial statements in the Annual Report and Accounts.

The AIRB models are largely based on the outcomes of credit risk (probability of default – PD) models. The Group's rating model is developed internally using statistical analysis and management judgement. In addition, exposures at default and loss given default models are in use. The models combine internal data supplemented with external data during model development.

The ratings system uses a through the cycle approach. The models are subject to rigorous oversight, governance and validation including, where appropriate, benchmarking to external information.

For retail reporting purposes, borrowers are also segmented into a number of risk bands, each representing a defined range of default probabilities. Exposures migrate between risk bands if the assessment of the borrowers' probability of default changes.

Each rating model is subject to a validation process, undertaken by an independent Risk team, which includes benchmarking to externally available data where possible. All rating models are approved by the Credit Risk Committee.

The PRA supplements the Group's minimum total capital requirement by setting additional Pillar 2 requirements issued within the Group's Individual Capital Guidance (ICG). This is added to the Pillar 1 requirement for those risks not covered or fully covered under Pillar 1. A key input into the PRA's ICG setting process is a bank's own assessment of the amount of capital it needs; this is known as the Internal Capital Adequacy Assessment process. The material Pillar 2 risks identified by the Group are credit concentration risk, operational risk, business risk (including transformation and reputation risk), interest rate risk in the banking book and underestimation of credit risk.

As part of the capital planning process, capital positions are subjected to stress testing and sensitivity analysis to determine the adequacy of capital resources against minimum requirements, including ICG, over the forecast period. The stress testing output is used by the PRA to set the overall capital requirement for the Group.

Full Analysis of Risk Classes

The Group has been set a specific ICG by the PRA and maintains capital at a level which exceeds this requirement The PRA requires the regulatory capital requirement to remain confidential between the Group and the PRA.

Mitigation

The Group has capital management procedures that are designed to ensure compliance with risk appetite and regulatory requirements and are positioned to meet anticipated future changes to capital requirements.

The Group is able to accumulate additional capital through profit retention by raising equity through, for example, a rights issue or debt exchange and by raising Tier 1 and Tier 2 capital by issuing subordinated liabilities. The cost and availability of additional capital is dependent upon market conditions and perceptions at the time. The Group is also able to manage the demand for capital through management actions including adjusting lending strategy, risk hedging strategies and through business disposals. If necessary, this can include limiting new business.

Monitoring

Capital is actively managed with regulatory ratios being a key factor in the Group's planning processes and stress analysis. A minimum of a three year forecast of the Group's capital position, based upon the strategic plan, is produced at least annually to inform the capital strategy. Shorter term forecasts are more frequently undertaken to understand and respond to variations of the Group's actual performance against the plan.

Capital plans are tested for capital adequacy using market-wide and idiosyncratic stress scenarios covering adverse economic conditions and other adverse factors that could impact the Group. The Group maintains mitigation and recovery options which set out a range of potential actions that could be taken in response to a stress.

Capital management is subject to independent oversight. Regular reporting of actual and projected ratios is undertaken, including submissions to the Asset and Liability Committee, the Risk Management Committee and the Board.

The regulatory framework within which the Group operates continues to be enhanced as part of the global banking reforms. Since the end of 2014, the Group reports its capital position on a fully loaded basis. The transitional provisions relating to adjustments to capital resources and requirements no longer apply.

Beyond CRD IV, there have been a number of draft technical standards issued for consultation which relate to both capital and leverage, and both Basel and European regulatory bodies continue to develop their thinking on capital resources and capital requirement measures. Within the UK, the PRA have been active in requiring enhanced capital standards and encouraging further disclosure developments. HM Treasury has been consulted on the practical aspects of the application of a countercyclical buffer.

The Group monitors these developments closely, participating in the regulatory consultation processes and analysing the potential financial impacts to ensure that the Group has a strong loss absorption capacity that exceeds the regulatory requirements.

Capital developments

CRD IV introduced new capital limits and buffers for banks, and includes a requirement to hold Common Equity Tier 1 capital to account for capital conservation, countercyclical and systemic risk buffers.

These new buffers will influence the type of capital instruments that best meet the requirements likely to be expected of the Group. Implementation is required from 2016. The Group reviews the capital structure on an on-going basis to ensure it is well placed to react to prevailing economic and regulatory conditions. From a capital perspective, the Common Equity Tier 1 capital ratio for the Group was 17.5% as at 31 December 2015, compared with a fully loaded regulatory minimum of 7.0% (comprised of Common Equity Tier 1 capital of 4.5% and a capital conservation buffer of 2.5%).

CRD IV also introduced a new leverage ratio requirement. The leverage ratio is a non-risk based measure that is designed to act as a supplement to risk based capital requirements. It is intended as a back stop measure. The leverage calculation determines a ratio based on the relationship between Tier 1 capital and total consolidated exposure (total exposure is the sum of on-balance sheet exposures, derivative exposures, securities financing transaction exposures and off-balance sheet items).

The leverage ratio for the Group (based on the Basel III definition of January 2014, and the revised CRD IV definition of October 2014) is 4.0%. There is no minimum requirement for the Group until it has deposits of £50 billion. To avoid capital cliffs the Group maintains a prudent risk appetite for leverage.

Risk Management Report

Full Analysis of Risk Classes

Ring-fencing is scheduled to be implemented fully into the UK banking system by 1 January 2019. The PRA has imposed a ring-fencing threshold of £25 billion retail deposits that the Group expects to breach before the proposed implementation date. On the assumption of organic growth and based on current business undertaken we expect the entire business will be within the ring-fence when it comes into effect at the beginning of 2019.

Minimum Requirements for Eligible Liabilities (MREL) are applicable from 1 January 2016 and will be phased in fully by 1 January 2020. Prior to 31 December 2019, MREL will be equal to an institution's minimum regulatory capital requirements. The Bank of England will provide prospective MREL guidance during 2016 to the Group, as well as guidance on the transitional arrangements until 1 January 2020. Once this is received the Group will work towards implementation of these requirements.

The framework for a Systemic Risk Buffer for ring-fenced banks will be applied to individual institutions by the PRA and will be introduced, like ring-fencing rules, from 2019. Given the scale of the Group it is likely to attract a Systemic Risk Buffer of 0%.

The table below shows the Group's capital resources.

	2015 £m	2014 £m
Common Equity Tier 1 (audited)		
Share capital and share premium account	**654.6**	654.6
Other equity instruments	**156.5**	156.5
Other reserves	**(15.6)**	(1.8)
Retained earnings	**544.8**	434.5
Total equity per balance sheet	**1,340.3**	1,243.8
Regulatory capital adjustments (unaudited)		
Deconsolidation of non regulated companies	**4.5**	4.1
Foreseeable distribution on Additional Tier 1 securities	**(2.1)**	(2.1)
Foreseeable distribution on ordinary shares	**(13.7)**	–
Other equity instruments	**(156.5)**	(156.5)
Cash flow hedge reserve	**15.3**	8.8
Intangible assets	**(64.4)**	(46.1)
Deferred tax on tax losses carried forward	**(18.0)**	(38.1)
Excess of expected loss over impairment	**(35.4)**	(33.4)
Common Equity Tier 1 capital	**1,070.0**	980.5
Additional Tier 1 securities	**156.5**	156.5
Total Tier 1 capital	**1,226.5**	1,137.0
Tier 2 capital (unaudited)		
General credit risk adjustments	**7.6**	5.9
Total Tier 2 capital	**7.6**	5.9
Total own funds	**1,234.1**	1,142.9

As required by Article 26(2) of the Capital Requirements Regulation, a deduction has been made for forseeable dividends on 2015 profits.

Full Analysis of Risk Classes

The table below shows movements in Common Equity Tier 1 capital.

(unaudited)	**2015 £m**	2014 £m
At 1 January	**980.5**	808.9
Movement in retained earnings	**110.3**	15.5
Net impact of share capital issue	**–**	145.4
Movement in available-for-sale reserve	**(7.3)**	0.5
Movements in foreseeable distribution on additional tier 1 securities	**–**	(2.1)
Movements in foreseeable distribution on ordinary shares	**(13.7)**	–
Exclude losses from non-regulated companies	**0.4**	0.6
Movement in intangible assets	**(18.3)**	(20.1)
Movement in excess of expected loss over impairment	**(2.0)**	7.7
Movement in deferred tax on tax losses carried forward	**20.1**	24.1
At 31 December	**1,070.0**	980.5

The main driver for the increase in capital resources is the increase in retained earnings, offset by expected distributions, and other items as set out in the table above.

The table below shows risk-weighted assets.

(unaudited)	**2015 £m**	2014 £m
Retail mortgages	**3,952.9**	3,489.7
Retail unsecured lending	**1,192.7**	830.0
Treasury	**229.0**	221.7
Other assets	**196.3**	175.0
Credit valuation adjustments	**14.3**	13.7
Operational risk	**525.2**	430.5
Total risk-weighted assets	**6,110.4**	5,160.6

The table below shows Pillar 1 risk-weighted assets and capital requirements by business line.

(unaudited)	**2015 Risk weighted assets £m**	**2015 Capital requirement £m**	2014 Risk weighted assets £m	2014 Capital requirement £m
Mortgages and savings	**4,284.5**	**342.8**	3,729.8	298.4
Credit cards	**1,334.7**	**106.8**	973.2	77.9
Current accounts, insurance and investments	**51.6**	**4.1**	47.2	3.7
Central functions	**439.6**	**35.1**	410.4	32.7
Total	**6,110.4**	**488.8**	5,160.6	412.7

Risk Management Report

Full Analysis of Risk Classes

Movement in risk-weighted assets

The Group uses a variable scalar methodology to calculate the probability of default (PD) used within the AIRB capital models. This approach aids capital management by ensuring the regulatory PD, and therefore the resultant regulatory capital requirements, fluctuate mainly due to changes in the credit quality mix of the portfolio, rather than changes in the economy. This methodology reduces, and does not eliminate, procyclicality within PD estimates. During 2015 the improvement in arrears rates and the increase in the proportion of accounts in the lowest risk bands have caused a reduction in the point-in-time PDs. These lower point-in-time PDs have resulted in the requirement to increase the scaling factor used to transform these to the long-run average estimates. It is these higher scaling factors, shown in the following table as 'model calibration', that resulted in increased RWAs of £46.1 million in 2015.

During 2015, changes were implemented within the AIRB models. The most significant change was to account for the growth in the House Price Index (HPI) beyond historic peak property prices in 2007. This change, combined with a minor change to the classification of accounts within the AIRB models is represented in the table below by 'model updates'.

In addition, further changes in the portfolio have been observed over the last 12 months. These impacts are included in the 'other movements' in the table, and attributed to:

- a change in the portfolio distribution across the PD model segments, from new business acquisitions and portfolio attrition, resulting in an increase in the regulatory PDs and the associated RWAs; and
- significant house price growth observed across the UK in 2015 which increased downturn loss given default, corresponding in a further increase in RWAs.

Operational risk is calculated using the Standardised Approach, based on the average Group income over the past three years. The year-on-year increase reflects the increasing Group income from 2011 to 2014.

(unaudited)	IRB mortgage £m	Standardised lending £m	Other standardised assets £m	Credit valuation adjustment £m	Operational risks £m	Total £m
RWAs at 1 January 2015	3,489.7	830.0	396.7	13.7	430.5	5,160.6
Book size	560.0	362.9	–	–	–	922.9
Model calibration	46.1	–	–	–	–	46.1
Model updates	(343.8)	–	–	–	–	(343.8)
Other movements	200.9	(0.2)	28.6	0.6	94.7	324.6
RWAs at 31 December 2015	**3,952.9**	**1,192.7**	**425.3**	**14.3**	**525.2**	**6,110.4**

Leverage ratio

CRD IV introduced a new balance sheet metric, the leverage ratio, as a requirement from 1 January 2014. The leverage ratio is risk insensitive, requiring capital to be held against total and off-balance sheet exposures such as undrawn credit facilities.

The Basel Committee is testing this ratio at a minimum threshold of 3.0% until 2017. The Group's leverage ratio as at 31 December 2015 was 4.0% (2014: 4.1%) as disclosed on page 207.

Exposure values associated with derivatives and securities financing transactions have been reported in compliance with CRD IV rules. For the purposes of the leverage ratio, the derivative measure is calculated as the replacement cost for the current exposure plus an add-on for potential future exposure. The exposure amount is not reduced for any collateral received from the counterparty and has been grossed up for any collateral provided.

Full Analysis of Risk Classes

Off-balance sheet items are made up of undrawn credit facilities. Credit conversion factors have been applied to these items to convert them to an on-balance sheet equivalent in compliance with the CRD IV rules.

Other regulatory adjustments consist of adjustments that have been applied to Tier 1 capital which are also applied to the leverage ratio exposure measure. This ensures consistency between Tier 1 capital and the total exposures components of the ratio.

(unaudited)	2015 £m	2014 £m
Tier 1 capital	**1,226.5**	1,137.0
Exposures measure		
Total regulatory balance sheet assets	**30,233.2**	26,540.6
Removal of accounting values for derivatives	**(82.3)**	(101.2)
Exposure value for derivatives	**61.8**	172.3
Exposure value for securities financing transactions	**261.7**	353.8
Off-balance sheet items	**659.5**	607.8
Other regulatory adjustments	**(102.5)**	(108.8)
Total exposures	**31,031.4**	**27,464.5**
Leverage ratio at 2015	**4.0%**	**4.1%**

Risk Management Report

Full Analysis of Risk Classes

31 December 2015 accounting reconciliation

(unaudited)	Accounting balance sheet as in published financial statements £m	Deconsolidation of other entities £m	Under regulatory scope of consolidation £m
Assets			
Cash and balances with central banks	888.6	–	888.6
Derivative financial instruments	82.3	–	82.3
Loans and receivables:			
Loans and advances to banks	614.5	(0.1)	614.4
Loans and advances to customers	27,109.0	–	27,109.0
Debt securities	1.1	–	1.1
Available-for-sale financial assets	1,296.9	–	1,296.9
Intangible assets	64.4	–	64.4
Tangible fixed assets	74.6	–	74.6
Deferred tax	38.0	–	38.0
Other assets	59.6	(0.4)	59.2
Intercompany assets	–	4.7	4.7
Total assets	30,229.0	4.2	30,233.2
Liabilities			
Deposits from banks	1,298.7	–	1,298.7
Customer deposits	25,144.9	–	25,144.9
Derivative financial instruments	156.0	–	156.0
Debt securities in issue	2,039.4	–	2,039.4
Provisions	8.4	(0.2)	8.2
Other liabilities	241.3	(0.1)	241.2
Total liabilities	28,888.7	(0.3)	28,888.4
Equity			
Share capital and share premium	654.6	–	654.6
Other equity instruments	156.5	–	156.5
Other reserves	(15.6)	–	(15.6)
Retained earnings	544.8	4.5	549.3
Total equity	1,340.3	4.5	1,344.8
Total liabilities and equity	30,229.0	4.2	30,233.2

Financial statements

Chelsea McClammer at the Virgin Money London Marathon 2015

Financial statements

Independent Auditor's Report to the members of Virgin Money Holdings (UK) plc only

Opinions and conclusions arising from our audit

1. Our opinion on the financial statements is unmodified

We have audited the financial statements of Virgin Money Holdings (UK) plc for the year ended 31 December 2015 set out on pages 214 to 282. In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent company's affairs as at 31 December 2015 and of the Group's profit for the year then ended;
- the Group financial statements have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU);
- the parent company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

2. Our assessment of risks of material misstatement

In arriving at our audit opinion above, we designed our audit procedures to reflect the risks we identified in the Group by performing increased procedures in the areas with most significant risk.

Our audit began with a risk assessment of the inherent risks facing the Group and how these are managed. This included understanding: the strength of the Group's capital and liquidity position; the impact of key strategic projects; the composition of its balance sheet; and the management of its cost base. We assessed and challenged the inherent risks with reference to:

- Our experience of the Group and the retail banking industry;
- The views of our specialists in a number of areas including regulation, IT and tax;
- The views of the Prudential Regulation Authority and Financial Conduct Authority; and
- The significant changes taking place in banking regulation in the UK.

We also considered the Group's control environment, including appropriate controls designed to prevent fraud.

The risk assessment highlighted the areas where significant judgement was required. As described on pages 103 to 104 these are also areas that have been focused on by the Group's Audit Committee. In forming our unmodified opinion on the financial statements, we undertook the following principal procedures on each of the areas as follows.

Allowance for impairment losses on loans and receivables (£39.9m)

Refer to page 103 (Audit Committee Report), pages 224, 231 and 232 (accounting policy) and note 8 (financial disclosures).

The risk: The impairment provision relating to secured and unsecured loans is one of the key judgemental areas for our audit due to the level of subjectivity inherent in estimating the impact of certain key assumptions on the recoverability of loan balances.

The Group performs an assessment of its loans for impairment, with the key assumptions being the probability of an account falling into arrears and subsequently defaulting, the emergence period, and the valuation of any recoveries expected to be made. For secured lending, the recoveries assessment includes the market valuations of collateral provided and the estimated time and cost to sell any property repossessed by the Group. For unsecured lending, the likelihood and amount of recoveries through sales to third parties is assessed. Due to the limited historical information available on actual default patterns and loss emergence periods and the fact that past performance is not necessarily an indication of future performance, there is a risk that the actual outcome is different from the probability assumed.

Our response: Our audit procedures included:

- We assessed the accuracy of the secured and unsecured impairment models by re-performing a sample of calculations performed by the impairment models and agreed a sample of data inputs, including the loans split by arrears status, to reports from the source systems. We assessed whether these reports were complete and accurate by checking the system codes used to extract the information.
- We compared the assumptions used in the impairment models to those approved by the Group. We critically assessed those assumptions against our understanding of the Group, the historical accuracy of its estimates, the current and past performance of the Group's loans and our knowledge of the industry in respect of these types of loans.

Independent Auditor's Report to the members of Virgin Money Holdings (UK) plc only

- We benchmarked the Group's assumptions, such as arrears trends, and the ratio between provisions and total/impaired loan balances against industry data, and compared macroeconomic variables such as house price inflation to market information.
- We tested the controls designed and applied by the Group to provide assurance that the assumptions explained above are regularly updated, that changes are monitored, scrutinised and approved by appropriate personnel and that the final assumptions used in the impairment models have been appropriately approved.
- We considered the adequacy of the Group's disclosures on impairment losses and key assumptions.

Recognition of revenue from secured and unsecured lending (£824.8m)

Refer to page 103 (Audit Committee Report), pages 222 and 231 (accounting policy) and note 3 (financial disclosures).

The risk: Interest earned on loans and receivables is recognised using the effective interest rate method which spreads the directly attributable cash flows, including transaction costs and discounts, over the expected lives of the instrument. The key assumptions in this calculation is the expected life of the instrument and the profile of the cash flows. The expected lives and usage patterns are informed by past customer behaviour, which demonstrates how and when customers have historically paid off their loans as well as spending patterns for unsecured loans. Judgement is used by the Group to convert this historical information into the assumptions of future behaviour included in the models. There is a risk that this judgement may not appropriately reflect all the facts available, which would skew the recognition of interest income.

Our response: Our audit procedures included:

- We agreed a sample of inputs into the models to source information, including comparing total secured loan balances to the loan system output and total unsecured balances to system reports.
- We used data tools to identify changes to the calculations used by the model and re-performed a sample of calculations performed to check their accuracy. We compared the methodology used to our interpretation of the requirements of the relevant accounting standards.
- We challenged the appropriateness of key assumptions, including the expected lives and usage patterns, by comparing these to historical expected life trends within the Group and to our own expectations based on our knowledge of the Group and experience of the industry in which it operates.
- We considered the adequacy of the Group's disclosures over revenue.

We continue to perform audit procedures over share based payments and capitalisation of project costs. However, due to the reduced complexity in the Group's share schemes and internal projects, we have not assessed these as being included in the risks that had the greatest effect on our audit and, therefore, they are not separately identified in our report this year.

3. Our application of materiality and an overview of the scope of our audit

The materiality for the Group financial statements as a whole was set at £6.0 million (2014: £6.0 million), determined with reference to a benchmark of profit before tax (2014: gross interest receivable plus non-funded income) of which it represents 4.3 per cent (2014: 0.7 per cent). We have considered profit before tax to be the most appropriate benchmark in the current year as profitability now reflects the scale of the business.

We report to the Audit Committee any uncorrected identified misstatements exceeding £0.3 million (2014: £0.3 million), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Our audits of the six components of the Group were performed by the audit team at the Group's central hubs that perform or support the key financial processes primarily in Edinburgh and Gosforth. The audit work undertaken at these two hubs was all performed by the Group auditor to materiality levels set individually for each component, which ranged from £0.1 million to £6.0 million. These Group audit procedures covered 100% of total Group revenue, Group profit before tax and total Group assets.

4. Our opinion on other matters prescribed by the Companies Act 2006 is unmodified

In our opinion:

- the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006; and
- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Independent Auditor's Report to the members of Virgin Money Holdings (UK) plc only

5. We have nothing to report on the disclosures of principal risks

Based on the knowledge we acquired during our audit, we have nothing material to add or draw attention to in relation to:

- the viability statement on pages 52 to 53, concerning the principal risks, their management, and, based on that, the directors' assessment and expectations of the group's continuing in operation over the 3 years to 31 December 2018; or
- the disclosures in note 1 of the financial statements concerning the use of the going concern basis of accounting.

6. We have nothing to report in respect of the matters on which we are required to report by exception

Under ISAs (UK and Ireland) we are required to report to you if, based on the knowledge we acquired during our audit, we have identified other information in the annual report that contains a material inconsistency with either that knowledge or the financial statements, a material misstatement of fact, or that is otherwise misleading.

In particular, we are required to report to you if:

- we have identified material inconsistencies between the knowledge we acquired during our audit and the directors' statement that they consider that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the Group's performance, business model and strategy; or
- the Audit Committee Report does not appropriately address matters communicated by us to the audit committee.

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements and the part of the Directors' Remuneration Report to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Under the Listing Rules we are required to review:

- the directors' statements, set out on page 135, in relation to going concern and longer-term viability; and
- the part of the Corporate Governance Statement on page 95 relating to the company's compliance with the eleven provisions of the 2014 UK Corporate Governance Code specified for our review.

We have nothing to report in respect of the above responsibilities.

Scope and responsibilities

As explained more fully in the Statement of Directors' Responsibilities set out on pags 137 to 138, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate. This report is made solely to the company's members as a body and is subject to important explanations and disclaimers regarding our responsibilities, published on our website at www.kpmg.com/uk/auditscopeukco2014a, which are incorporated into this report as if set out in full and should be read to provide an understanding of the purpose of this report, the work we have undertaken and the basis of our opinions.

John Ellacott (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London
E14 5GL

1 March 2016

Consolidated income statement

For the year ended 31 December

	Note	2015 £ million	2014 £ million
Interest and similar income		**839.3**	771.6
Interest and similar expense		**(384.5)**	(404.3)
Net interest income	3	**454.8**	367.3
Fee and commission income		**27.4**	35.1
Fee and commission expense		**(1.2)**	(1.1)
Net fee and commission income	4	**26.2**	34.0
Other operating income	5	**41.3**	36.9
Fair value (losses)/gains on financial instruments	13	**(0.4)**	0.1
Other income		**67.1**	71.0
Total income		**521.9**	438.3
Other operating expenses	6	**(353.6)**	(338.9)
Fees associated with listing		**–**	(12.6)
Total operating expenses	6	**(353.6)**	(351.5)
Profit before tax from operating activities		**168.3**	86.8
Impairment	8	**(30.3)**	(15.8)
Gain on sale of subsidiary	19	**–**	4.5
Additional Northern Rock consideration		**–**	(36.0)
Premium on repurchase of Non-core Tier 1 notes in issue		**–**	(4.5)
Loss for the period of disposal group		**–**	(1.0)
Profit before tax		**138.0**	34.0
Taxation	9	**(26.8)**	(25.3)
Profit for the year		**111.2**	8.7
Profit attributable to equity owners		**111.2**	8.7
Profit for the year		**111.2**	8.7
Basic earnings per share (pence)	10	**22.9**	(0.4)
Diluted earnings per share (pence)	10	**22.7**	(0.4)

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated statement of comprehensive income

For the year ended 31 December

	Note	**2015 £ million**	2014 £ million
Profit for the year		**111.2**	8.7
Other comprehensive income *Items that may subsequently be reclassified to profit or loss:*			
Movements in revaluation reserve in respect of available-for-sale financial assets:			
Change in fair value	31	**25.1**	12.1
Income statement transfers in respect of disposals	31	**(33.6)**	(10.3)
Taxation	31	**1.2**	(1.3)
		(7.3)	0.5
Movements in cash flow hedge reserve:			
Effective portion of changes in fair value taken to other comprehensive income	31	**(13.2)**	(14.1)
Net income statement transfers	31	**5.1**	2.6
Taxation	31	**1.6**	2.5
		(6.5)	(9.0)
Other comprehensive expense for the year, net of tax		**(13.8)**	(8.5)
Total comprehensive income for the year		**97.4**	0.2

Total comprehensive income attributable to equity owners		**97.4**	0.2

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated balance sheet

As at 31 December

	Note	**2015 £ million**	2014 £ million
Assets			
Cash and balances at central banks		**888.6**	851.3
Derivative financial instruments	13	**82.3**	101.2
Loans and receivables:			
– Loans and advances to banks	14	**614.5**	720.5
– Loans and advances to customers	15	**27,109.0**	23,093.1
– Debt securities		**1.1**	8.6
		27,724.6	23,822.2
Available-for-sale financial assets	16	**1,296.9**	1,539.6
Intangible assets	20	**64.4**	46.1
Tangible fixed assets	21	**74.6**	72.9
Deferred tax assets	22	**38.0**	50.2
Other assets	23	**59.6**	53.3
Total assets		**30,229.0**	26,536.8

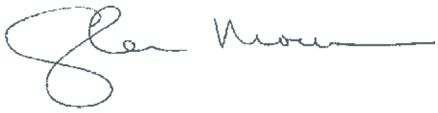
Consolidated balance sheet

As at 31 December

Equity and liabilities	Note	2015 £ million	2014 £ million
Liabilities			
Deposits from banks	24	**1,298.7**	846.7
Customer deposits	25	**25,144.9**	22,365.7
Derivative financial instruments	13	**156.0**	228.2
Debt securities in issue	26	**2,039.4**	1,594.1
Provisions	27	**8.4**	9.3
Other liabilities	28	**241.3**	249.0
Total liabilities		**28,888.7**	25,293.0
Equity			
Share capital and share premium	29	**654.6**	654.6
Other equity instruments	30	**156.5**	156.5
Other reserves	31	**(15.6)**	(1.8)
Retained earnings	32	**544.8**	434.5
Total equity		**1,340.3**	1,243.8
Total liabilities and equity		**30,229.0**	26,536.8

The accompanying notes are an integral part of these consolidated financial statements.

The financial statements were approved and authorised for issue by the Board and were signed on its behalf on 1 March 2016.



Glen Moreno
Chairman

Jayne-Anne Gadhia CBE
Chief Executive

Consolidated statement of changes in equity

For the year ended 31 December

Attributable to equity holders

	Share capital and share premium £ million	Other equity instruments £ million	Other reserves £ million	Retained earnings £ million	Total equity £ million
Balance at 1 January 2015	654.6	156.5	(1.8)	434.5	1,243.8
Comprehensive income					
Profit for the year	–	–	–	111.2	111.2
Other comprehensive income					
Net movement in available-for-sale reserve	–	–	(7.3)	–	(7.3)
Net movement in cash flow hedge reserve	–	–	(6.5)	–	(6.5)
Total other comprehensive expense	–	–	(13.8)	–	(13.8)
Total comprehensive (expense)/income for the year	–	–	(13.8)	111.2	97.4
Transactions with equity holders					
Share based payments – charge for the year	–	–	–	20.0	20.0
Deferred tax on share based payments	–	–	–	0.3	0.3
Purchase of own shares	–	–	–	(5.0)	(5.0)
Distribution to Additional Tier 1 security holders	–	–	–	(12.6)	(12.6)
Group relief attributable to Additional Tier 1 securities	–	–	–	2.6	2.6
Dividends paid to ordinary shareholders	–	–	–	(6.2)	(6.2)
Total transactions with equity holders	–	–	–	(0.9)	(0.9)
Balance at 31 December 2015	654.6	156.5	(15.6)	544.8	1,340.3

Further details of movements in the Group's share capital and reserves are provided in notes 29, 30, 31 and 32.

Consolidated statement of changes in equity

For the year ended 31 December

Attributable to equity holders (continued)

	Share capital and share premium £ million	Other equity instruments £ million	Other reserves £ million	Retained earnings £ million	Total equity £ million
Balance at 1 January 2014	509.2	–	6.7	419.0	934.9
Comprehensive income					
Profit for the year	–	–	–	8.7	8.7
Other comprehensive income					
Net movement in available-for-sale reserve	–	–	0.5	–	0.5
Net movement in cash flow hedge reserve	–	–	(9.0)	–	(9.0)
Total other comprehensive income	–	–	(8.5)	–	(8.5)
Total comprehensive (expense)/income for the year	–	–	(8.5)	8.7	0.2
Transactions with equity holders					
Share based payments – charge for the year	–	–	–	12.9	12.9
Share based payments – reclassifications from liabilities	–	–	–	4.2	4.2
Issue of ordinary shares (net)	145.4	–	–	–	145.4
Issue of Additional Tier 1 securities (net)	–	156.5	–	–	156.5
Distribution to Additional Tier 1 security holders	–	–	–	(3.2)	(3.2)
Distribution to Non-core Tier 1 noteholders	–	–	–	(9.2)	(9.2)
Group relief attributable to Tier 1 securities	–	–	–	2.1	2.1
Total transactions with equity holders	145.4	156.5	–	6.8	308.7
Balance at 31 December 2014	654.6	156.5	(1.8)	434.5	1,243.8

Further details of movements in the Group's share capital and reserves are provided in notes 29, 30, 31 and 32.

Consolidated cash flow statement

For the year ended 31 December

	Note	2015 £ million	2014 £ million
Profit before taxation		**138.0**	34.0
Adjustments for:			
Changes in operating assets	35(a)	**(4,037.3)**	(2,330.6)
Changes in operating liabilities	35(b)	**3,146.4**	1,805.6
Non-cash and other items	35(c)	**62.4**	(132.8)
Tax paid		**(5.0)**	–
Net cash used in operating activities		**(695.5)**	(623.8)
Cash flows from investing activities			
Net investment in intangible assets		**(29.5)**	(26.9)
Purchase of fixed assets		**(10.2)**	(10.6)
Disposal of fixed assets		**–**	(0.2)
Net investment in securities		**(659.2)**	(956.5)
Proceeds from sale and redemption of securities		**900.5**	1,278.5
Movement in disposal group assets and liabilities		**–**	7.7
Net investment in credit card portfolio		**–**	(362.7)
Net cash flow from disposal of Church House Trust Limited		**–**	11.5
Net cash provided by/(used in) investing activities		**201.6**	(59.2)
Cash flows from financing activities			
Distributions to Tier 1 noteholders		**(12.6)**	(20.2)
Repayment of Non-core Tier 1 notes		**–**	(154.5)
Net proceeds from issue of debt securities		**1,047.2**	998.4
Repayments of debt securities in issue		**(601.9)**	(874.1)
Proceeds from issue of Additional Tier 1 securities (net)		**–**	156.5
Proceeds from issue of ordinary shares (net)		**–**	145.4
Purchase of own shares		**(5.0)**	–
Dividends paid to ordinary shareholders	11	**(6.2)**	–
Payment of additional Northern Rock consideration		**–**	(50.0)
Net cash provided by financing activities		**421.5**	201.5
Change in cash and cash equivalents		**(72.4)**	(481.5)
Cash and cash equivalents at beginning of year		**1,533.8**	2,015.3
Cash and cash equivalents at end of year	35(d)	**1,461.4**	1,533.8

The accompanying notes are an integral part of these consolidated financial statements.

Notes to the consolidated financial statements

Note 1: Basis of preparation

1.1 Reporting entity

Virgin Money Holdings (UK) plc (the Company) is a public limited company incorporated and registered in England and Wales. The registered office is Jubilee House, Gosforth, Newcastle-Upon-Tyne, NE3 4PL.

The Company was incorporated on 4 August 1995 as a private limited company with registered number 03087587. On 24 July 2014 the Company was re-registered as a public limited company.

The Company is the parent entity and the ultimate controlling party of the Virgin Money Group (the Group).

1.2 Basis of preparation

The Group consolidated financial statements, which should be read in conjunction with the Directors' Report, have been prepared on a going concern basis in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS.

The Directors have reviewed the strategic plan which shows the financial position, cash flow, liquidity and capital forecasts for the Group. The Directors are confident that the Group will have sufficient resources to meet its liabilities as they fall due. Accordingly the Directors believe that it remains appropriate to prepare the financial statements on a going concern basis.

1.3 Changes in accounting policy

New standards, amendments to standards and interpretations adopted

The following amendment to IFRS 13 is mandatory for annual reporting periods beginning on or after 1 January 2015, has been endorsed for adoption by the EU and has been adopted by the Group during the year ended 31 December 2015:

Pronouncement	Impact of change
Amendment to IFRS 13 'Fair value measurement'	The amendment clarifies that the portfolio exception in IFRS 13, which allows an entity to measure the fair value of a group of financial assets and financial liabilities on a net basis, applies to all contracts (including non-financial contracts) within the scope of IAS 39 or IFRS 9. This amendment did not have a significant impact on the Group when adopted.

There are no other standards, amendments to standards or interpretations that are applicable in the year which have a material impact on these financial statements.

New accounting standards issued by the IASB which are effective in future periods are presented in note 39.

1.4 Presentation of information

Presentation of risk disclosures

Disclosures under IFRS 7 'Financial Instruments: Disclosure' concerning the nature and extent of risks relating to financial instruments have been included within the audited sections of the Risk Management Report. Where marked as 'audited' these are covered by the Independent Auditor's Report.

1.5 Basis of consolidation

The Group consists of the Company and its subsidiaries. The subsidiaries are listed in note 3 of the parent company financial statements. The consolidated financial statements comprise the financial statements of the Group.

Entities are regarded as subsidiaries where the Group has the power over an investee, exposure or rights to variable returns from its involvement with the investee and the ability to affect those returns. Inter-company transactions and balances are eliminated upon consolidation. Subsidiaries are consolidated from the date on which control is transferred to the Group and are deconsolidated from the date that power over an investee, exposure or rights to variable returns and the ability to affect these returns ceases. Accounting policies are applied consistently across the Group.

The Virgin Money Foundation, launched in August 2015, is managed and controlled by a Board of independent Trustees, such that the Group has no power over the Foundation or, exposure or ability to affect variable returns. The Foundation is therefore not consolidated in the financial statements of the Group.

Special Purpose Vehicles (SPV) are entities created to accomplish a narrow and well defined objective. For the Group this is the securitisation of mortgage assets. An SPV is consolidated if the Group has control over the SPV, is exposed to rights of variable returns from its involvement in the SPV and has the ability to affect those returns through its power over the entity.

1.6 Basis of measurement

The financial statements have been prepared under the historical cost convention as modified by the revaluation of derivative financial instruments, available-for-sale and other assets held at fair value through profit or loss. A summary of the material accounting policies of the Group are included within note 1.9. Policies which are relevant to the financial statements as a whole are set out below.

The accounting policies set out in the note 1.9 have been applied consistently to all periods presented in these financial statements.

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

1.7 Client money

The Group's unit trust management and investment intermediary subsidiaries administer money on behalf of some clients in accordance with the Client Money Rules of the Financial Conduct Authority. Client money is not recognised in the balance sheet or in the notes to the financial statements as the Group is not the beneficial owner.

1.8 Foreign currency translation

The Group's financial statements are presented in sterling, which is the functional currency of the Company, all of its subsidiaries and the SPVs included within the consolidated financial statements.

Foreign currency transactions are translated into functional currency using the exchange rates prevailing at the dates of the transactions. Monetary items denominated in foreign currencies are translated at the rate prevailing at the balance sheet date. Foreign exchange gains and losses resulting from the restatement and settlement of such transactions are recognised in the income statement, except when recognised in other comprehensive income if relating to a qualifying cash flow hedge or available-for-sale assets. Non-monetary items (which are assets or liabilities which do not attach to a right to receive or an obligation to pay currency) measured at amortised cost and denominated in foreign currencies are translated at the exchange rate at the date of the transaction. Non-monetary items measured at fair value are translated at the exchange rate at the date of valuation. Where these are held at fair value through the income statement, exchange differences are reported as part of the fair value gain or loss.

1.9 Accounting policies

The accounting policies of the Group are set out below.

(a) Operating segments

The Group determines operating segments according to similar economic characteristics and the nature of its products and services in accordance with IFRS 8 'Operating Segments'. Management reviews the Group's internal reporting based around these segments in order to assess performance and allocate resources.

Segment performance is evaluated based on underlying profit or loss and is measured consistently with underlying profit or loss in the consolidated financial statements (income tax is unallocated). Segment results are regularly reviewed and reported to the Board of Directors to allocate resources to segments and to assess their performance.

Operating segments are reported in a manner consistent with the internal reporting provided to the Board. The Group Executive Committee (management) has been determined to be the chief operating decision maker for the Group.

(b) Interest income and expense

Interest income and expense are recognised in the income statement for all instruments measured at amortised cost using the effective interest rate method.

This method calculates the amortised cost of a financial asset or liability, and allocates the interest income or expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or, where appropriate, a shorter period to the net carrying amount of the financial asset or liability. The Group estimates cash flows considering all contractual terms of the financial instrument (for example prepayment options) but does not consider future credit losses. The calculation includes all amounts received or paid by the Group that are an integral part of the overall return, direct incremental transaction costs related to the acquisition or issue of a financial instrument and all other premiums and discounts.

Once a financial asset or group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Interest receivable or payable on derivatives, whether in economic or accounting hedges, is recorded on an accruals basis in interest receivable or payable. Interest on available-for-sale (AFS) debt securities is recorded in interest receivable using the effective interest rate method.

(c) Fees and commissions

Where they are not included in the effective interest rate calculation, fees and commissions are recognised on an accruals basis when the service has been received or provided. Loan commitment fees for loans that are likely to be drawn down are deferred (together with related incremental direct costs) and recognised as an adjustment to the effective interest rate on the loan.

Fee income from general insurance and life insurance policies is recognised in full on the effective date of commencement or renewal of the related policies to reflect underlying contracts with product providers.

(d) Other operating income

Other operating income comprises the fair value for services, net of value added tax, rebates and discounts. Other operating income is attributable to the sale and management of stocks and shares ISAs, pensions, authorised unit trusts, the marketing of credit cards and other financial services products.

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

Other operating income from sales of units in managed funds is recognised daily based on the average volume of funds under management.

Fees charged to charities for registering with Virgin Money Giving are recognised from the date on which recovery is reasonably certain. The commission charged on donations and event fees is recognised from the date donations and event fees are transacted on the website. Both of these income streams contribute towards costs incurred by Virgin Money Giving.

Other income includes commission on donations, interest received from related parties and other sundry income.

The Group recognises ongoing credit card income from strategic partners as other income.

(e) Total operating expenses

Operating expenses are recognised on an accruals basis as services are provided. Included within the employee benefits expense are employee share based payments. The accounting policy in relation to share based payments is set out in policy (f).

Staff costs

The Group accounts for components of employee costs on the following bases:

› Short-term employee benefits

Short term employee benefits include salaries and social security costs and are recognised over the period in which the employees provide the services to which the payments relate.

Cash bonus awards are recognised to the extent that the Group has a present obligation to its employees that can be measured reliably and are recognised over the period of service that employees are required to work to qualify for the payment.

› Other long-term employee benefits

Other long-term employee benefits include deferred cash bonus awards. Deferred cash bonus awards are recognised at the present value of the obligation at the reporting date. These costs are recognised over the period of service that employees are required to work to qualify for the payment.

› Retirement benefit obligations

A defined contribution plan is a post-employment benefit plan into which the Group pays fixed contributions and has no legal or constructive obligation to pay further amounts. Contributions are recognised as staff expenses in profit or loss in the periods during which related employee services are fulfilled.

The Group operates defined contribution pension schemes for its Directors and employees. The assets of the schemes are held separately from those of the Group in independently administered funds.

The accounting policies for employee share based payments are set out in policy (f).

Leases

If the lease agreement in which the Group is a lessee transfers the risks and rewards of the asset, the lease is recorded as a finance lease and the related asset is capitalised. At inception, the asset is recorded at the lower of the present value of the minimum lease payments or fair value and is depreciated over the estimated useful life. The lease obligations are recorded as borrowings.

If the lease does not transfer the risks and rewards of the asset, the lease is recorded as an operating lease.

Operating lease payments are charged to profit or loss on a straight line basis over the lease term unless a different systematic basis is more appropriate. Where an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor in compensation is charged to profit or loss in the period in which termination is made.

(f) Share based payments

The Group puts in place share schemes for employees to reward strong long-term business performance and to incentivise growth for the future.

The Group engages in equity and cash settled share based payment transactions in respect of services received from certain of its employees.

For equity settled share based payment transactions the grant date fair value of the award is recognised as an employee expense with a corresponding increase in equity over the period that the employees become unconditionally entitled to the awards.

The grant date fair value of the award is determined using valuation models which take into account the terms and conditions attached to the awards. Inputs into valuation models may include the exercise price, the risk-free interest rate, the expected volatility of the Company's share price and other various factors which relate to performance conditions attached to the awards.

The amount recognised as an expense is adjusted to reflect the actual number of awards for which the related service and non-market vesting conditions are expected to be met such that the amount ultimately recognised as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date.

For share based payment awards with market performance conditions or non-vesting conditions the grant date fair

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

value of the award is measured to reflect such conditions and there is no true-up for differences between expected and actual outcomes.

For cash settled share based payment transactions the fair value of the amount payable to the employee is recognised as an expense with a corresponding increase in liabilities. The fair value is initially measured at grant date and spread over the period during which the employees become unconditionally entitled to payment. The fair value is measured based on a valuation model taking into account the terms and conditions of the grant. The liability is revalued at each balance sheet date and settlement date with any changes to fair value being recognised in profit or loss.

(g) Impairment losses

The Group assesses its financial assets or groups of financial assets for objective evidence of impairment at each balance sheet date. An impairment loss is recognised if a loss event (or events) has occurred after initial recognition, and on or before the balance sheet date, that has a reliably measurable impact on the estimated future cash flows of the financial assets or groups of financial assets. Losses incurred as a result of events occurring after the balance sheet date are not recognised in these financial statements.

- **Assets held at amortised cost**

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. Objective evidence that a financial asset is impaired includes observable data that comes to the attention of the Group about the following loss events:

- there is evidence of the customer or issuer experiencing financial difficulty;
- there is a breach of contract, such as a default or delinquency in repayments;
- the customer is granted a concession that would otherwise not be considered;
- the borrower will enter bankruptcy or other financial reorganisation;
- the disappearance of an active market for that financial asset because of financial difficulties; and
- observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the portfolio, including:
  - there are adverse changes in the payment status of borrowers in the portfolio; and
  - economic conditions that correlate with defaults on the assets in the portfolio.

If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. In assessing collective impairment the Group uses statistical modelling of historic trends to assess the probability of a group of financial assets going into default and the subsequent loss incurred. Regular model monitoring is performed to ensure model assumptions remain appropriate.

Assets that are individually assessed and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and receivables has been incurred, the amount of the loss is measured as the difference between the asset carrying amount and the present value of the estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an impairment allowance and the amount of the loss is recognised in profit or loss.

When a loan or receivable is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are recognised directly in the income statement. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the customer's credit rating), the previously recognised impairment loss is reversed by adjusting the impairment allowance. The amount of the reversal is recognised in profit or loss.

A provision is also made in the case of accounts, which may not currently be in arrears, where losses may have been incurred but not yet recognised. An increased level of provision is held for accounts where an impairment trigger event has occurred which includes accounts benefiting from forbearance and those in arrears. Refer to page 156 of the Risk Management Report for details of the forbearance policy.

(h) Taxation

Taxation comprises current tax and deferred tax. Current tax and deferred tax are recognised in profit or loss except to the extent that they relate to items recognised directly in equity

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

or other comprehensive income. Current tax is based on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years. The Group has adopted the Code of Practice on Taxation for Banks issued by HM Revenue and Customs.

Further disclosures relating to deferred tax are included in policy (s).

(i) Earnings per share

Basic earnings per share is calculated by dividing the profit attributable to ordinary shareholders of the parent company by the weighted-average number of ordinary shares outstanding during the period excluding own shares held in employee benefit trusts or held for trading.

The diluted earnings per share is calculated by adjusting the profit or loss that is attributable to ordinary shareholders and the weighted-average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise share options granted to employees.

For the calculation of diluted earnings per share the weighted-average number of ordinary shares in issue is adjusted to assume conversion of all dilutive potential ordinary shares, if any, that arise in respect of share options and rewards granted to employees. The number of shares that could have been acquired at the average annual share price of the Company's shares based on the monetary value of the subscription rights attached to outstanding share options and awards is determined. This is deducted from the number of shares issuable under such options and awards to leave a residual bonus amount of shares which are added to the weighted-average number of ordinary shares in issue, but no adjustment is made to the profit attributable to equity shareholders.

(j) Financial instruments

Financial assets

Financial assets can be classified in the following categories:

- loans and receivables;
- available-for-sale;
- held to maturity; or
- financial assets at fair value through profit or loss.

Management determines the classification of its financial instruments at initial recognition. The Group measures all of its financial liabilities at amortised cost, other than derivatives and those instruments which have been designated as part of a hedging relationship (refer policy (n)). Purchases and sales of financial assets at fair value through profit or loss, held to maturity and available-for-sale are recognised on the trade date, the date on which the Group commits to purchase or sell the asset.

Loans and receivables at amortised cost

The Group's loans and advances to banks and customers and some investment securities are classified as loans and receivables. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, whose recoverability is based solely on the credit risk of the customer and where the Group has no intention of trading the loan or receivable. Loans and receivables are initially recognised at fair value including direct and incremental transaction costs. Subsequent recognition is at amortised cost using the effective interest rate method, less any provision for impairment.

Available-for-sale financial assets

Available-for-sale financial assets are non-derivative assets that are either designated as available-for-sale or are assets that do not meet the definition of loans and receivables and are not derivatives or assets held at fair value through profit or loss. These are principally but not exclusively investment securities intended to be held for an indefinite period of time which may be sold in response to a need for liquidity or changes in interest rates, exchange rates or equity prices. They are initially measured at fair value including direct and incremental transaction costs. Fair values are obtained from quoted market prices in active markets and, where these are not available, from valuation techniques including discounted cash flow models (refer to policy (m)). With the exception of unquoted equity instruments measured at cost less impairment because their fair value cannot be measured reliably, subsequent measurement is at fair value, with changes in fair value being recognised in other comprehensive income except for impairment losses and translation differences, which are recognised in profit or loss. Upon derecognition of the asset, or where there is objective evidence that the investment security is impaired, the cumulative gains and losses recognised in other comprehensive income are removed from other comprehensive income and recycled to profit or loss.

Held to maturity financial assets

Held to maturity financial assets are non-derivative financial assets with fixed or determinable payments that the Group has the ability and intention to hold to maturity. They are initially measured at fair value including direct and incremental transaction costs. Subsequent measurement is at amortised cost using the effective interest rate method. No financial assets were classified as held to maturity during either the current or prior year.

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

Financial assets at fair value through profit or loss

This category consists of derivative financial assets. Assets in this category are carried at fair value. The fair values of derivative instruments are calculated by discounted cash flow models using yield curves that are based on observable market data or are based on valuations obtained from counterparties. Gains and losses arising from the changes in the fair values are recognised in profit or loss.

The fair values of quoted investments in active markets are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

Financial liabilities

Borrowings, including deposits and debt securities in issue are recognised initially at fair value, being the issue proceeds net of premiums, discounts and transaction costs incurred. All borrowings are subsequently measured at amortised cost using the effective interest rate method. Amortised cost is adjusted for the amortisation of any premiums, discounts and transaction costs. The amortisation is recognised in interest expense and similar charges using the effective interest rate method. The Group does not hold any financial liabilities classified as held for trading.

Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

Sale and repurchase agreements

Securities sold subject to repurchase agreements (repos) are reclassified in the financial statements as assets pledged when the transferee has the right by contract or custom to sell or repledge the collateral. The counterparty liability is included in amounts due to other banks, deposits from banks, other deposits or deposits due to customers, as appropriate. Securities purchased under agreements to resell (reverse repos) are recorded as loans and advances to banks or customers as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest rate method. Securities lent to counterparties are also retained in the financial statements.

Derecognition of financial assets and liabilities

Derecognition is the point at which the Group removes an asset or liability from its balance sheet. The Group's policy is to derecognise financial assets only when the contractual right to the cash flows from the financial asset expires or when the Group transfers the financial assets to another party provided the transfer of the asset also transfers the right to receive the cash flows of the financial asset or where the Group has transferred substantially all the risks and rewards of ownership. Where the transfer does not result in the Group transferring the right to receive the cash flows of the financial assets, but it does result in the Group assuming a corresponding obligation to pay the cash flows to another recipient, the financial assets are also accordingly derecognised. The Group derecognises financial liabilities only when the obligation specified in the contract is discharged, converted to shares, cancelled or has expired or is transferred to a third party. There were no transactions in the year where the Group transferred financial assets that should have been derecognised in their entirety.

(k) Loans and advances to banks

The Group's loans and advances to banks are classified as loans and receivables.

(l) Loans and advances to customers

The Group's loans and advances to customers are classified as loans and receivables.

Further details of the application of the effective interest rate method are included in policy (b) and provision for impairment in policy (g).

(m) Available-for-sale financial assets

Debt securities are designated as either available-for-sale or loans and receivables. Debt securities are principally available-for-sale as they are intended to be held for an indefinite period of time but may be sold in response to a need for liquidity or changes in interest rates, exchange rates or equity prices. Debt securities classified as loans and receivables are asset backed securities for which there is no active market.

The Group's debt securities, treasury bills and equity instruments are classified as available-for-sale assets. For available-for-sale financial assets, the Group assesses at each balance sheet date whether there is objective evidence that a financial asset, or group of financial assets are impaired. The amount of the loss is measured as the difference between the asset's acquisition cost less principal repayments and amortisation and the current fair value. The amount of the impairment loss is recognised in profit or loss. This includes cumulative gains and losses previously recognised in other comprehensive income which are recycled from other comprehensive income to the income statement. If, in a subsequent period, the fair value of an instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through profit or loss.

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

(n) Derivative financial instruments and hedge accounting

The Group is authorised to undertake the following types of derivative financial instrument transactions for non-trading purposes: cross currency swaps, interest rate swaps, equity swaps, interest rate caps, forward rate agreements, options, foreign exchange contracts and similar instruments.

The Group's derivative activities are entered into for the purpose of matching or eliminating risk from potential movements in interest rates, foreign exchange rates and equity exposures inherent in the Group's assets, liabilities and positions. All derivative transactions are for economic hedging purposes and it is decided at the outset which position the derivative will be hedging. Derivatives are reviewed regularly for their effectiveness as hedges and corrective action taken, if appropriate. Derivatives are measured initially at fair value and subsequently remeasured to fair value. Fair values are obtained from quoted market prices in active markets and, where these are not available, from valuation techniques including discounted cash flow models and option pricing models. Where derivatives are not designated as part of a hedging relationship, changes in fair value are recorded in the income statement. Where derivatives are designated within hedging relationships, the treatment of the changes in fair value depends on the nature of the hedging relationship as explained below.

Hedge accounting is used for derivatives designated in this way provided certain criteria are met. The Group documents at the inception of the hedge relationship the link between the hedging instrument and the hedged item as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment both at hedge inception and on an ongoing basis of whether the derivatives used in hedging transactions are highly effective in offsetting changes in the fair values or cash flows of hedged items. The Group designates certain derivatives as either:

- **Cash flow hedges**

A cash flow hedge is used to hedge exposures to variability in cash flows, such as variable rate financial assets and liabilities. The effective portion of changes in the derivative fair value is recognised in other comprehensive income, and recycled to the income statement in the periods when the hedged item will affect profit and loss. Interest rate derivatives designated as cash flow hedges primarily hedge the exposure to cash flow vulnerability from forecast loans and advances to customers. The fair value gain or loss relating to the ineffective portion is recognised immediately in profit or loss.

- **Fair value hedges**

A fair value hedge is used to hedge exposures to variability in the fair value of financial assets and liabilities, such as fixed rate loans. Changes in fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of the hedged item is amortised to the income statement over the period to maturity.

The most frequently used fair value hedges are:

- hedging the interest rate risk of a portfolio of prepayable fixed rate assets with interest rate derivatives. This solution is used to establish a macro fair value hedge for derivatives hedging fixed rate mortgages;
- hedging the interest rate risk of a portfolio of fixed rate liabilities with interest rate derivatives. This solution is used to establish a macro fair value hedge for derivatives hedging fixed rate savings;
- hedging the interest rate risk of a portfolio of non-prepayable fixed rate assets with interest rate derivatives. This solution is used to establish a macro fair value hedge for fixed rate investments; and
- hedging the interest rate and foreign currency exchange risk of non-prepayable, foreign currency denominated fixed rate assets or liabilities on a one-for-one basis with fixed/floating or floating/fixed cross currency interest rate swaps.

(o) Securitisation transactions

Certain Group companies have issued debt securities in order to finance specific loans and advances to customers. Both the debt securities in issue and the loans and advances to customers remain on the Group balance sheet within the appropriate balance sheet headings unless:

- a fully proportional share of all or of specifically identified cash flows have been transferred to the holders of the debt securities, in which case that proportion of the assets are derecognised;
- substantially all the risks and rewards associated with the assets have been transferred, in which case the assets are fully derecognised; and
- a significant proportion of the risks and rewards have been transferred, in which case the assets are recognised only to the extent of the Group's continuing involvement.

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

The Group has also entered into self-issuance of securitised debt which may be used as collateral for repurchase or similar transactions. Investments in self-issued debt and the equivalent deemed loan, together with the related income, expense and cash flows, are eliminated on consolidation in the financial statements.

› Debt securities in issue

Issued securities are classified as liabilities where the contractual arrangements result in the Group having an obligation to deliver either cash or another financial asset to the security holder, or to exchange financial instruments under conditions that are potentially unfavourable to the Group. Issued securities are classified as equity where they meet the definition of equity and confer a residual interest in the Group's assets on the holder of the securities.

Financial liabilities are carried at amortised cost using the effective interest rate method (see policy (j)). Equity instruments are initially recognised at net proceeds, after deducting transaction costs and any related income tax. Appropriations to holders of equity securities are deducted from equity, net of any related income tax, as they become irrevocably due to the holders of the securities.

Securitisation is a means used by the Group to fund an element of its mortgage portfolio. These securitised advances are subject to non-recourse finance arrangements. These advances have been transferred at their principal value to Special Purpose Vehicles (SPV) and have been funded through the issue of amortising mortgage backed securities to investors.

As discussed in note 1.5, the Group controls the securitisation SPVs and therefore consolidates the assets and liabilities of the securitisation SPVs, on a line by line basis.

(p) Business combinations

Business combinations are accounted for using the acquisition method as at the acquisition date, being when control is transferred to the Group. Control is having the power over an investee, exposure or rights to variable returns from its involvement with the investee and the ability to use its power to affect those returns.

The Group measures goodwill at the acquisition date as the fair value of the consideration transferred less the fair value of the net identifiable assets acquired and liabilities assumed.

When the excess is negative, the negative goodwill is recognised immediately in profit or loss.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in profit or loss.

Transaction costs, other than those associated with the issue of debt or equity securities, that the Group incurs in connection with a business combination are expensed as incurred.

Any contingent consideration payable is measured at fair value at the acquisition date. If the contingent consideration is classified as equity, then it is not remeasured and settlement is accounted within equity. Otherwise, subsequent changes in the fair value of the contingent consideration are recognised in profit or loss.

(q) Intangible assets and amortisation

Intangible assets purchased separately from a business combination are capitalised at their cost and amortised from the date from which they become available for use over their useful economic life which is generally 3 to 10 years. Intangible assets acquired as part of an acquisition are capitalised at their fair value where this can be measured reliably in accordance with IFRS 13 'Fair Value Measurement'.

Expenditure incurred in relation to scoping, planning and researching the build of an asset as part of a project is expensed as incurred.

Development expenditure incurred on a project is capitalised only if the following criteria are met:

- an asset is created that can be identified;
- it is probable that the asset created will generate future economic benefits; and
- the development cost of the asset can be measured reliably.

Following the initial recognition of development expenditure, the cost is amortised over the estimated useful lives of the assets created. Amortisation commences on the date that the asset is brought into use.

Internally generated intangible assets relate to computer software and core banking platforms.

› Computer software

Costs incurred in acquiring and developing computer software for internal use are capitalised as intangible assets where the software leads to the creation of an identifiable non-monetary asset and it is probable that the expected future economic benefits that are attributable to the asset will flow to the Group from its use for a period of over one year. The software is classified as an intangible asset where it is not an integral part of the related hardware and amortised over its estimated useful life on a straight line basis which is generally 3 to 10 years.

Costs associated with maintaining software are expensed as they are incurred.

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

Core deposit intangible

The core deposit intangible was recognised on acquisition of Northern Rock plc (now renamed Virgin Money plc). It was recognised in respect of the intrinsic value of the retail savings book acquired. This will be amortised over its remaining useful life of one year.

Goodwill

Purchased goodwill (representing the excess of the fair value of the consideration given over the fair value of the separable net assets acquired) arising on business combinations in respect of acquisitions since 1 January 1998 is capitalised.

Positive goodwill is held on the balance sheet and tested for impairment annually.

Core banking platforms

Core banking platforms primarily represent the construction of core operating platforms, which are internally generated. Core banking platforms are amortised on a straight line basis over 3 to 10 years.

Impairment of intangible assets

Intangible assets are assessed for indications of impairment at each balance sheet date, or more frequently where required by events or changes in circumstances. If indications of impairment are found, these assets are subject to an impairment review. The impairment review compares the carrying value of the assets with their recoverable amounts, which are defined as the higher of the fair value less costs to sell and their value in use. Fair value less costs to sell is the amount at which the asset could be sold in a binding agreement in an arm's length transaction. Value in use is calculated as the discounted cash flows generated as a result of the asset's continued use including those generated by its ultimate disposal, discounted at a market rate of interest on a pre-tax basis.

Where impairments are indicated, the carrying values of intangible assets are written down by the amount of the impairment and the charge is recognised in the income statement in the period in which it occurs. A previously recognised impairment charge on a fixed asset may be reversed in full or in part where a change in circumstances leads to a change in the estimates used to determine its recoverable amount. The carrying value of the intangible asset will only be increased to the carrying value at which it would have been held had the impairment not been recognised.

(r) Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost less accumulated depreciation and provision for impairment, as appropriate. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for its intended use. Additions and subsequent expenditure are included in the asset's carrying value or are recognised as a separate asset only when they improve the expected future economic benefits to be derived from the asset. All other repairs and maintenance are charged to the income statement in the period in which they are incurred.

Depreciation is provided using the straight line method to allocate costs less residual values over estimated useful lives, as follows:

Freehold property	50-100 years
Leasehold property	Unexpired period of the lease
Plant and leasehold improvements	5-30 years
Computer equipment	3-5 years
Office equipment	3-10 years
Motor vehicles	4 years

The residual values and useful lives of assets are reviewed, and adjusted if appropriate, at each balance sheet date. Where the cost of freehold land can be identified separately from buildings, the land is not depreciated. Tangible fixed assets are subject to impairment testing, as appropriate.

Impairment of tangible fixed assets

Tangible fixed assets are assessed for indications of impairment at each balance sheet date, or more frequently where required by events or changes in circumstances. If indications of impairment are found, these assets are subject to an impairment review. The impairment review compares the carrying value of the assets with their recoverable amount, which are defined as the higher of the fair value less costs to sell and their value in use. Fair value less costs to sell is the amount at which the asset could be sold in a binding agreement in an arm's length transaction. Value in use is calculated as the discounted cash flows generated as a result of the asset's continued use including those generated by its ultimate disposal, discounted at a market rate of interest on a pre-tax basis.

Where impairments are indicated, the carrying values of fixed assets are written down by the amount of the impairment and the charge is recognised in the income statement in the period in which it occurs. A previously recognised impairment charge on a fixed asset may be reversed in full or in part where a change in circumstances leads to a change in the estimates used to determine its recoverable amount. The carrying value of the fixed asset will only be increased to the carrying value at which it would have been held had the impairment not been recognised.

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

(s) Deferred tax

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

Deferred tax assets are recognised for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

(t) Other assets

Other assets include prepayments and other amounts the Group is due to receive from third parties in the normal course of business.

(u) Deposits from banks

Deposits by banks are initially measured at fair value, which is normally the proceeds received net of any directly attributable transaction costs incurred. Subsequent measurement is at amortised cost, using the effective interest rate method.

(v) Customer deposits

Customer deposits are initially measured at fair value, which is normally the proceeds received. Subsequent measurement is at amortised cost, using the effective interest rate method.

(w) Provisions

Provisions are recognised for present obligations arising from past events where it is more likely than not that an outflow of resources will be required to settle the obligations and they can be estimated reliably.

A provision for bank levies is recognised when the condition that triggers the payment of the levy is met. If a levy obligation is subject to a minimum activity threshold so that the obligating event is reaching a minimum activity, then a provision is recognised when that minimum activity threshold is reached.

(x) Other liabilities

Deferred income represents amounts received in advance of the Group providing services, and will be recognised as income in profit or loss when the services have been provided.

Other creditors represent amounts the Group is due to pay to third parties in the normal course of business. These include expense accruals, which have been incurred, but not yet billed.

Accrued expenses are amounts that the Group is due to pay to third parties in the normal course of business.

(y) Share capital and share premium

Share capital

The financial instruments issued by the Company are treated as equity (i.e. forming part of shareholders' funds) only to the extent that they meet the following two conditions:

- they include no contractual obligations upon the Company to deliver cash or other financial assets or to exchange financial assets or financial liabilities with another party under conditions that are potentially unfavourable to the Group; and
- where the instrument will or may be settled in the Company's own equity instruments, it is either a non-derivative that includes no obligation to deliver a variable number of the Company's own equity instruments or is a derivative that will be settled by the Company exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

To the extent that this definition is not met, the proceeds of issue are classified as a financial liability.

Share issue costs

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Dividends and appropriations

Dividends are recognised in equity in the period in which they are approved by the Company's shareholders or paid.

Share premium

Share premium substantially represents the aggregate of all amounts that have ever been paid above par value to the Company when it has issued ordinary and non-voting Ordinary Shares. Certain expenses in relation to the issue of share capital can be offset against the share premium account. These expenses must be the incremental expenses arising on issue of the shares.

(z) Other equity instruments

Issued financial instruments are recognised as equity where there is no contractual obligation to deliver either cash or another financial asset. The proceeds are included in equity, net of transaction costs. Dividends and other returns to equity holders are treated as a deduction from equity.

(aa) Other reserves

Available-for-sale reserve

The available-for-sale reserve represents the unrealised change in the fair value of available-for-sale investments since initial recognition.

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

Cash flow hedge reserve

For derivatives designated in a cash flow hedge, the effective portion of changes in fair value is recognised in the cash flow hedge reserve and recycled to profit or loss in the periods when the hedged item will affect profit or loss.

(ab) Contingent liabilities

Contingent liabilities are possible obligations whose existence depends upon the outcome of uncertain future events or are present obligations where the outflows of resources are uncertain or cannot be reliably measured. Contingent liabilities are not recognised in the financial statements but are disclosed unless they are remote.

(ac) Fair value of financial assets and liabilities

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

For the majority of instruments, fair value is determined with reference to quoted prices in an active market. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

Refer to note 34 for a description of different levels within the fair value hierarchy. Levels are reviewed at each balance sheet date and this determines where transfers between levels are required.

Where quoted prices are not available, fair value is based upon cash flow models, which use wherever possible independently sourced observable market parameters such as interest rate yield curves, currency rates and option volatilities. The chosen valuation technique incorporates all the factors that market participants would take into account in pricing a transaction and is discounted at a risk free rate.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of consideration given or received. The Group does not apply a credit valuation adjustment (CVA) or debit valuation adjustment (DVA) to reflect the credit risk of its derivative exposures as the Group's portfolio is fully collateralised.

If an asset or a liability measured at fair value has a bid price and an ask price, the Group measures assets and long positions at bid price and liabilities and short positions at an ask price.

Portfolios of financial assets and financial liabilities that are exposed to market risk and credit risk that are managed by the Group on the basis of the net exposure to either market or credit risk, are measured on the basis of a price that would be received to sell a net long position (or transferred to sell a net short position) for a particular risk exposure. Those portfolio risk adjustments are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

1.10 Critical estimates and judgements

The preparation of financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, actual results ultimately may differ from those estimates.

The areas involving a higher degree of judgement or complexity, or where assumptions and estimates are significant to the 2015 financial statements were as follows:

(a) Effective interest rates

IAS 39 requires interest earned from mortgages and credit cards to be measured under the effective interest rate method. Management must therefore use judgement to estimate the expected life of each instrument and hence the expected future cash flows relating to it. The accuracy of the effective interest rate would therefore be affected by unexpected market movements resulting in altered customer behaviour, inaccuracies in the models or incorrect assumptions.

If the estimated life of secured loans were increased or reduced by one month, the value of such loans on the balance sheet would be increased or decreased by £3.6 million (2014: £2.5 million) and £3.7 million (2014: £2.6 million) respectively.

If the estimated life of credit cards were increased or reduced by one month, the value of such assets on the balance sheet would be increased or decreased by £1.1 million (2014: £0.6 million) and £1.1 million (2014: £0.5 million) respectively.

(b) Impairment of loans and receivables

Individual impairment losses on secured loans and advances are calculated based on an individual valuation of the underlying asset. Collective impairment losses on loans and advances are calculated using a statistical model.

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

The key assumptions used in the model are the probability of default; the probability of this default resulting in possession and/or write off; and the subsequent loss incurred. These key assumptions are monitored regularly to ensure the impairment allowance is entirely reflective of the current portfolio.

The accuracy of the impairment calculation would therefore be affected by unanticipated changes to the economic environment and assumptions which differ from actual outcomes. For mortgage loan receivables to the extent that:

- the loss given default differs by +/- 10%, for example if the loss given default is 10% then it is increased to 11%, the impairment allowance would be an estimated £0.3 million (2014: £0.2 million) higher or £0.3 million (2014: £0.2 million) lower respectively;
- the level of house prices differs by +/- 10%, for example a property value of £100,000 is increased to £110,000, the impairment allowance would be an estimated £1.3 million (2014: £0.7 million) lower or £3.0 million (2014: £3.4 million) higher respectively;
- the emergence period of 6 months differs by +/- 3 months, the impairment allowance would be an estimated £0.2 million (2014: £0.1 million) higher or £0.2 million (2014: £0.1 million) lower respectively.

For credit card receivables, to the extent that the loss given default differs by +/- 10%, the impairment allowance would be an estimated £2.9 million (2014: £2.7 million) higher or £2.9 million (2014: £2.7 million) lower respectively, and to the extent the emergence period of 6 months differs by +/-3 months, the impairment allowance would be an estimated £3.8 million (2014: £2.0 million) higher or £3.8 million (2014: £2.0 million) lower respectively.

(c) Capitalisation and impairment of intangibles

Intangibles are initially recognised when they are separable or arise from contractual or other legal rights, the cost can be measured reliably and, in the case of intangible assets not acquired in a business combination, where it is probable that future economic benefits attributable to the assets will flow from their use. Management review and monitor the capitalisation of significant project development costs on a regular basis to ensure that they meet the recognition criteria for capitalisation of an intangible asset and to ensure the costs are directly attributable to the individual projects where an asset is under construction. A review of capitalisation of intangibles has been undertaken to ensure these conditions have been met.

A review of intangible assets which are not yet in use for indications of impairment is undertaken at each reporting date. If there are indicators of impairment, an estimate of the recoverable amount is made. The recoverable amount of the asset is the higher of its fair value less costs to sell and its value in use. Value in use is calculated by discounting the future cash flows (both costs to complete and benefits post completion) generated from the continuing use of the asset. If the carrying value of the asset is less than the greater of the value in use and the fair value less costs to sell, an impairment charge is recognised.

Through their assessment of intangible assets and review for impairment indicators Management have not identified any assets that have an impairment, therefore a £nil impairment charge has been recognised (2014: £nil).

(d) Deferred tax

Taxation involves estimation techniques to assess the liability in terms of possible outcomes. The assessment of the recoverability or otherwise of deferred tax assets is based mainly on a determination of whether the relevant entity will generate sufficient profits within 5 years to realise the deferred tax assets.

This is reviewed at each reporting date by the Directors with a detailed exercise conducted to establish the validity of profit forecasts and other relevant information including timescales over which the profits are expected to arise and the deferred tax assets will reverse. Deferred tax is determined using tax rates that have been enacted or substantially enacted by the balance sheet date and which are expected to apply when the related deferred tax assets are realised or the deferred tax liabilities are settled.

The judgement required in the assessment of whether to recognise deferred tax assets is set out in policy (s). A deferred taxation asset in respect of the subsidiary Virgin Money plc was not recognised at acquisition on 1 January 2012 but subsequently recognised because in the period since acquisition, Management have taken certain actions to have greater certainty about the profitability going forward.

Based on their interpretation of the timing and level of reversal of existing taxable temporary differences, in line with relevant accounting standards, the Directors conclude that a net deferred tax asset of £38.0 million (2014: £50.2 million) should be recognised at the balance sheet date.

Notes to the consolidated financial statements

Note 1: Basis of preparation (continued)

(e) Fair value of financial assets and liabilities

Management must use judgement and estimates calculating fair value where not all necessary inputs are observable or where factors specific to the Group's holdings need to be considered. The accuracy of the fair value calculations would therefore be affected by unexpected market movements, inaccuracies within the models used compared to actual outcomes and incorrect assumptions. For example, if Management were to use a tightening in the credit spread of ten basis points, the fair values of liabilities (including derivatives) would increase from the reported fair values by £25.7 million (2014: £23.3 million).

Estimates and judgements significant to the 2014 financial statements

The following were considered as estimates and judgements significant to the financial statements for the year ended 31 December 2014:

› Fair value of share based payments

The fair values of share awards granted in 2014 were calculated using statistical models, requiring application of management judgement on the inputs to these models. The nature of schemes with awards granted in 2015 are such that there is a reduced degree of judgement and complexity in calculations for the 2015 financial statements.

› Tax uncertainty

The degree of judgement and uncertainty involved in determining the Group's provision for income taxation, deferred taxation assets and liabilities and potential taxation liabilities was more significant in 2014. The ultimate outcome of certain tax matters is considered more certain.

› Disposal group classification and measurement

The Group fully disposed of its interests in Church House Trust (CHT) on 30 November 2014 and there are no disposal group assets or liabilities recognised at 31 December 2014 or 31 December 2015.

› Provisions and contingent liabilities

Provision values and determining whether to recognise contingent liabilities are both based on the best information available at the reporting date, and the degree of judgement and uncertainty is not considered as significant as in 2014.

› Additional Northern Rock consideration

The final payment to HM Treasury in respect of additional consideration of £50.0 million was made in 2014. With no further payments to come, no estimation uncertainty exists.

Additional information on the above estimates and judgements is provided in the Virgin Money Group Annual Report and Accounts 2014.

Notes to the consolidated financial statements

Note 2: Operating segments

Segmental reporting

For Management reporting purposes, the Group is organised into the following business groupings:

- Mortgages and savings;
- Credit cards;
- Current accounts, insurance and investments; and
- Central functions.

These business groupings reflect how the Executive assesses performance and makes decisions regarding the allocation of resources to the business on the basis of product and customers. Internal and external sources of revenue are allocated to the appropriate business segment.

Mortgages and savings

Mortgage products include Residential and Buy-to-Let mortgages. The Group also participates in the Help to Buy Scheme and the Help to Buy Equity Loan Scheme. The savings products currently include ISAs, easy access and fixed term accounts.

Credit cards

The Credit Card business was previously delivered through a successful partnership with MBNA. In March 2015 the Group successfully migrated over 675,000 customer accounts to its own platform. This resulted in an in-house capability to issue credit cards and manage the portfolio. The Group's credit card manufacturing capability was developed in partnership with leading credit card systems provider TSYS.

The capability of the new platform allows the Group to respond to market conditions more quickly and better align products to customer needs. The Group will continue its presence in the balance transfer market and further diversify the product range.

Current accounts, insurance and investments

Current accounts, insurance and investments include current accounts and other financial products. Other financial products are those offered beyond the core products of savings, mortgages and credit cards and include investments, international money transfers, travel money, pensions, life insurance, travel insurance, home insurance, motor insurance and pet insurance.

Central functions

Central functions provide shared support services to each of the Group's business lines and Virgin Money Giving (VMG). These services include information technology and property along with central services such as Risk, Finance, Human Resources and Management. It is not the policy of the Group to allocate the cost of these shared services to each business line. All depreciation and amortisation is allocated to the central functions business line.

The Group does not manage Treasury as a profit centre, and so the interest expense incurred from its Group funding and liquidity operations has been allocated to the other business lines. Treasury is not engaged in trading activities. Central functions segment assets and liabilities includes fixed assets and treasury assets and liabilities.

Due to the nature of the Group's operations there are no inter-segmental transactions.

Notes to the consolidated financial statements

Note 2: Operating segments (continued)

	Mortgages and savings £m	Credit cards £m	Current accounts, insurance and investments £m	Central functions £m	Underlying basis total £m
Year ended 31 December 2015					
Net interest income	**358.5**	**97.6**	**–**	**–**	**456.1**
Other income	**2.5**	**18.0**	**36.6**	**9.9**	**67.0**
Total underlying income	**361.0**	**115.6**	**36.6**	**9.9**	**523.1**
Total costs	**(92.7)**	**(37.1)**	**(16.7)**	**(186.0)**	**(332.5)**
Impairment	**(3.0)**	**(27.3)**	**–**	**–**	**(30.3)**
Underlying profit/(loss) before tax	**265.3**	**51.2**	**19.9**	**(176.1)**	**160.3**
Segment assets	**25,457.9**	**1,585.2**	**2.3**	**3,183.6**	**30,229.0**
Segment liabilities	**25,063.3**	**4.0**	**235.5**	**3,585.9**	**28,888.7**

	Mortgages and savings £m	Credit cards £m	Current accounts, insurance and investments £m	Central functions[1] £m	Underlying basis total £m
Year ended 31 December 2014					
Net interest income	291.0	75.1	–	–	366.1
Other income	3.1	25.2	32.8	11.0	72.1
Total underlying income	294.1	100.3	32.8	11.0	438.2
Total costs	(85.7)	(40.5)	(13.5)	(177.9)	(317.6)
Impairment	(1.2)	(14.6)	–	–	(15.8)
Underlying profit/(loss) before tax	207.2	45.2	19.3	(166.9)	104.8
Segment assets	22,005.6	1,112.8	3.6	3,414.8	26,536.8
Segment liabilities	22,322.6	4.8	202.5	2,763.1	25,293.0

1 The FSCS Levy was previously excluded from underlying performance measures, but is now included in central functions as it is considered to be a recurring cost to the Group.

Notes to the consolidated financial statements

Note 2: Operating segments (continued)

Reconciliation of statutory results to underlying basis

The underlying basis is the basis on which financial information is presented to the chief operating decision maker which excludes certain items included in the statutory results. The table below reconciles the statutory results to the underlying basis.

		Adjusted for					
					Costs associated with listing		
	Virgin Money Group statutory £m	Compensation for senior leavers £m	Strategic items £m	Fair value adjustments £m	Share based payments £m	Fees associated with listing £m	Underlying basis total £m
Year ended 31 December 2015							
Net interest income	**454.8**	**–**	**–**	**1.3**	**–**	**–**	**456.1**
Other income	**67.1**	**–**	**–**	**(0.1)**	**–**	**–**	**67.0**
Total income	**521.9**	**–**	**–**	**1.2**	**–**	**–**	**523.1**
Total operating expenses	**(353.6)**	**3.7**	**7.4**	**(0.5)**	**10.5**	**–**	**(332.5)**
Profit before tax from operating activities	**168.3**	**3.7**	**7.4**	**0.7**	**10.5**	**–**	**190.6**
Impairment	**(30.3)**	**–**	**–**	**–**	**–**	**–**	**(30.3)**
Profit before tax	**138.0**	**3.7**	**7.4**	**0.7**	**10.5**	**–**	**160.3**

		Adjusted for				
				Costs associated with listing		
	Virgin Money Group statutory £m	Strategic items £m	Fair value adjustments £m	Share based payments £m	Fees associated with listing £m	Underlying basis total[1] £m
Year ended 31 December 2014						
Net interest income	367.3	–	(1.2)	–	–	366.1
Other income	71.0	–	1.1	–	–	72.1
Total income	438.3	–	(0.1)	–	–	438.2
Total operating expenses	(351.5)	9.0	1.0	11.3	12.6	(317.6)
Profit before tax from operating activities	86.8	9.0	0.9	11.3	12.6	120.6
Impairment	(15.8)	–	–	–	–	(15.8)
Gain on sale of subsidiary	4.5	(4.5)	–	–	–	–
Additional Northern Rock consideration	(36.0)	36.0	–	–	–	–
Premium on repurchase of Non-core Tier 1 notes	(4.5)	4.5	–	–	–	–
Loss for the year of disposal group	(1.0)	1.0	–	–	–	–
Profit before tax	34.0	46.0	0.9	11.3	12.6	104.8

1 The FSCS Levy was previously excluded from underlying performance measures, but is now included in central functions as it is considered to be a recurring cost to the Group.

Geographical areas

As the Group's operating activities are exclusively in the UK, further analysis is not provided.

Notes to the consolidated financial statements

Note 3: Net interest income

Net interest income comprises:

	2015 £m	2014[1] £m
Interest and similar income:		
Loans and advances to customers	**822.4**	751.8
Loans and advances to banks	**2.4**	1.7
Debt securities classified as loans and receivables	**–**	0.1
Interest receivable on loans and receivables	**824.8**	753.6
Available-for-sale financial assets	**10.5**	11.5
Cash and balances at central banks	**4.0**	5.9
Other interest	**–**	0.6
Total interest and similar income	**839.3**	771.6
Interest and similar expense:		
Deposits from banks including liabilities under sale and repurchase agreements	**(6.8)**	(3.3)
Customer deposits	**(342.7)**	(373.3)
Debt securities in issue	**(29.0)**	(23.6)
Other	**(6.0)**	(4.1)
Total interest and similar expense	**(384.5)**	(404.3)
Net interest income	**454.8**	367.3

1 Items within interest income and expense have been reclassified to better reflect the interest bearing assets and liabilities to which they relate.

Interest accrued on individually impaired assets was £6.8 million (2014: £6.8 million).

Note 4: Net fee and commission income

Net fee and commission income comprises:

	2015 £m	2014 £m
Fee and commission income:		
On loans and advances to customers	**21.0**	28.9
Other fee and commission income	**6.4**	6.2
Total fee and commission income	**27.4**	35.1
Fee and commission expense:		
Other fee and commission expense	**(1.2)**	(1.1)
Net fee and commission income	**26.2**	34.0

Other fee and commission expense includes bank servicing costs and bank charges.

Notes to the consolidated financial statements

Note 5: Other operating income

Other operating income comprises:

	2015 £m	2014 £m
Investment income	**31.5**	28.7
Gain on sale of available-for-sale assets (refer note 16)	**8.8**	7.5
Other	**1.0**	0.7
Total other operating income	**41.3**	36.9

Total other operating income is derived in the United Kingdom and relates to trade with third parties and continuing operations.

Note 6: Total operating expenses

Total operating expenses comprise:

	2015 £m	2014 £m
Staff costs		
Salaries	**138.9**	125.6
Social security costs	**16.2**	14.3
Other pension costs	**10.6**	9.6
Employee share option schemes	**20.0**	13.5
	185.7	163.0
Premises and equipment		
Hire of equipment	**4.6**	4.8
Rent and rates	**9.0**	8.5
	13.6	13.3
Other expenses		
Marketing costs	**22.3**	16.5
FSCS levy	**12.5**	16.4
Professional fees	**10.7**	8.5
Other	**89.2**	106.4
	134.7	147.8
Depreciation and amortisation		
Depreciation of tangible fixed assets	**8.4**	8.0
Amortisation of intangible assets	**11.2**	6.8
	19.6	14.8
Total other operating expenses	**353.6**	338.9
Fees associated with listing	**–**	12.6
Total operating expenses	**353.6**	351.5

Notes to the consolidated financial statements

Note 6: Total operating expenses (continued)

Average headcount

The monthly average number of persons (including Directors) employed by the Group was as follows:

	2015	2014
Full time	**2,359**	2,244
Part time	**699**	660
Total	**3,058**	2,904

Retirement benefit obligations

The Group operates defined contribution pension schemes for its Directors and employees. The assets of the schemes are held separately from those of the Group in independently administered funds.

The Group made contributions of £10.5 million (2014: £9.6 million) during the year. There were no contributions overdue at the year end (2014: £nil).

Fees payable to the auditor

During the year the Group obtained the following services from the Group's auditor as detailed below:

	2015 £m	2014 £m
Fees payable for the audit of the current year annual report and accounts	**0.3**	0.2
Fees payable for other services:		
Audit of the subsidiaries pursuant to legislation	**0.6**	0.7
Total audit fees	**0.9**	0.9
Audit-related assurance services	**0.2**	0.2
Total audit and audit-related fees	**1.1**	1.1
Services relating to taxation:		
Taxation services	**–**	0.2
Total taxation related fees	**–**	0.2
Other non-audit fees:		
Services relating to corporate finance transactions	**–**	1.3
Other assurance services	**0.2**	0.7
Total other non-audit fees	**0.2**	2.0
Total fees payable to the auditor by the Group	**1.3**	3.3

All amounts are shown exclusive of VAT.

The following types of services are included in the categories listed above:

Audit and audit-related fees

This category includes fees in respect of the audit of the Group's annual financial statements and other services in connection with regulatory filings and services for assurance and related services that are reasonably related to the performance of the audit or review of the financial statements.

Other non-audit fees

Included within the total other non-audit fees of £2.0 million within 2014 are fees in relation to the listing of the Group which totalled £1.9 million exclusive of VAT.

Notes to the consolidated financial statements

Note 7: Share based payments

Share based payments charges comprise:

	2015 £m	2014 £m
Equity settled	**20.0**	12.9
Cash settled	**–**	0.6
Total share based payment charge	**20.0**	13.5

The scheme details are summarised below.

Equity settled schemes

	Award plan	Eligible employees	Nature of award	Vesting conditions[1]	Issue dates[2]
(A)	IPO incentive scheme	Selected senior employees	Conditional share award	Continuing employment or leavers in certain circumstances	2013
(B)	Phantom share award	Selected senior employees	Deferred bonus – conditional share award	Continuing employment or leavers in certain circumstances	2012 & 2013
(C)	Recruitment award	Two senior employees	Conditional share award	Continuing employment or leavers in certain circumstances	2013
(D)	Long-term incentive plan	Selected senior employees	Conditional share award	Continuing employment or leavers in certain circumstances and achievement of performance conditions	2015
(E)	IPO share award	All employees excluding the Group's Executive Committee	Conditional share award	Continuing employment or leavers in certain circumstances	2014
(F)	Deferred bonus share plan	Selected senior employees	Deferred bonus – conditional share award	Continuing employment or leavers in certain circumstances	2014 & 2015

1 All awards have vesting conditions and therefore some may not vest.

2 Issue dates show the year in which issues have been made under the relevant scheme. There could be further issuances in future years under the scheme.

The terms of the equity settled schemes the Group operated during the year are as follows:

(A) IPO incentive scheme

The IPO incentive scheme was introduced in December 2013 for selected senior employees. Participants were entitled to receive shares in the event of a listing. The award was a pre-determined percentage of the listing value, which was then converted to a number of Ordinary Shares based on the listing price. The fair value of the IPO incentive scheme was determined at grant date using a binomial valuation model and is being recorded in the income statement over the vesting period.

During 2014 modifications were made to the scheme including removal of the minimum listing market value. The impact of each modification was determined at the modification date and is being recorded in the income statement over the remaining vesting period.

(B) Phantom share award

In late 2012 a notional (phantom) share award for senior individuals was established. The plan was designed to comply with PRA requirements for deferral and clawback on treatment of variable remuneration. In 2013 the award was a cash payment based on Tangible Net Asset Value (TNAV) and was accounted for as a long-term employee benefit.

During 2014 the Remuneration Committee approved that existing awards under this scheme would be converted into Ordinary Shares awards on listing, with no acceleration of vesting. This resulted in a change in accounting treatment to an equity settled share based payment therefore during 2014 the Group reclassified an existing liability of £4.2 million to equity. The fair value of the converted award was recalculated and is being recognised over the remaining vesting period within the income statement through to 2018.

Notes to the consolidated financial statements

Note 7: Share based payments (continued)

(C) Recruitment award

Under the scheme the participants received shares in 2014 and 2015 and will receive the final tranche of shares in 2016. No awards were granted in 2015 (2014: none) under this scheme.

(D) Long-term incentive plan (LTIP)

The LTIP introduced in 2014 is aimed at delivering shareholder value by linking the receipt of shares to performance measures that are based on delivering the Group's strategic objectives over a 3 year period. Awards are made within limits set by the rules of the plan. The maximum number of shares that can be awarded equates to 120% of total annual remuneration under normal circumstances.

During 2015, selected senior employees of the Group were granted up to a maximum of 1,494,125 Ordinary Shares under the LTIP scheme. To the extent that performance measures are satisfied, the LTIP awards will vest equally on the third, fourth and fifth anniversary of the date of the grant. The performance period is three years commencing on 1 January 2015.

Details of the performance measures and weightings can be found in the Directors' Remuneration Report on page 135 of the 2014 Annual Report and Accounts. All performance measures are non-market based conditions. For each performance measure, if performance reaches threshold, target or maximum, then 20%, 80% or 100% respectively of this element of the award will vest. Vesting between threshold, target and maximum will be calculated on a straight line basis.

During 2015, awards over 233,645 Ordinary Shares were granted under this scheme to three senior employees on recruitment. The awards were granted in recognition that the employees' outstanding awards over shares in their previous employing company lapsed on accepting employment with the Group. Vesting dates replicate those of the forfeited awards. One of the awards is subject to performance conditions. The performance measures mirror those attached to the 2015 LTIP grant discussed above, however in recognition of the earlier vesting dates in March 2016 and March 2017, performance will be assessed against the Group's strategic plan for financial years 2015 and 2016 respectively.

The weighted-average fair value of awards granted during 2015 was £4.04 based on market prices at the date of grant. Participants may be entitled to any dividends paid during the vesting period if the performance measures and service conditions are met.

(E) IPO share award

On listing, the Group granted all employees below Executive level a one-off share award. A small number of senior employees received an award over Ordinary Shares of either 10% or 20% of salary. All other employees received an award over Ordinary Shares with a value of £1,000. The majority of awards vested on the first anniversary of the listing. Certain awards granted to senior employees were subject to different vesting schedules, and holding periods, to comply with the PRA Remuneration Code.

(F) Deferred bonus share plan

The deferred bonus share plan is an equity settled scheme that is operated in conjunction with the short term incentive plan for Executive Directors and other senior managers of the Group.

Share awards for the deferred element of 2015 bonuses will be granted under this scheme in 2016. During 2015, awards over 1,960,273 Ordinary Shares for 2014 bonuses were granted to selected senior employees of the Group. The awards have service conditions, with vesting dates in 2015, 2018 and 2019.

During 2015, awards over 72,410 Ordinary Shares were granted under the scheme to three senior employees on recruitment. The awards were granted in recognition that the employees' outstanding awards over shares in their previous employing company lapsed on accepting employment with the Group. The awards have service conditions and vesting dates replicate those of the forfeited awards.

The weighted-average fair value of awards granted during 2015 was £4.04 based on market prices at the date of grant. Participants may be entitled to any dividends paid during the vesting period if the service conditions are met.

Cash settled schemes

In 2015 there were no cash settled shared based payment schemes.

During 2014 cash payments of £1.7 million were made in relation to cash settled share based payment schemes, resulting in a charge of £0.6 million to the income statement for the year ended 31 December 2014.

Notes to the consolidated financial statements

Note 7: Share based payments (continued)

Movement in share options and conditional shares

	Ordinary Shares			
	Former Chairman's interest in share options[1]	Recruitment award[2]	Phantom share award[2]	IPO share award[2]
Shares in existence at 1 January 2015	625,328	327,760	3,120,900	1,773,880
Granted in year	–	–	–	–
Exercised or vested in year	–	(151,950)	–	(1,431,866)
Forfeited in year	–	–	(59,080)	(202,973)
Outstanding 31 December 2015	625,328	175,810	3,061,820	139,041
Of which exercisable	625,328	–	–	–

	Ordinary Shares		
	Long-term incentive plan[2]	Deferred bonus share plan[2]	IPO incentive scheme[2]
Shares in existence at 1 January 2015	–	14,918	664,658
Granted in year	1,727,770	2,032,683	–
Exercised or vested in year	(95,075)	(761,247)	(332,324)
Less: forfeited in year	(233,242)	(128,554)	–
Outstanding at 31 December 2015	1,399,453	1,157,800	332,334
Of which exercisable	–	–	–

1 This scheme was set up for the previous Chairman, Sir David Clementi. All share options granted under the scheme had vested as at 31 December 2014. No share options have been exercised during 2015. The weighted-average exercise price for options outstanding at 1 January 2015 and 31 December 2015 was £2.15. The options outstanding will expire 10 years from the date of listing if not exercised.

2 Awards have vesting conditions.

Notes to the consolidated financial statements

Note 7: Share based payments (continued)

	Ordinary Shares				
	Former Chairman's interest in share options[1]	Employee share award plan	Recruitment award[2]	Phantom share award[2]	IPO share award[2]
Shares in existence at 1 January 2014	65,824	104,232	39,014	–	–
Modification to Phantom share award	–	–	–	312,090	–
Impact of share reorganisation[3]	592,416	871,911	294,984	2,808,810	–
Granted in year	–	–	–	–	1,773,880
Exercised or vested in year	(32,912)	(968,790)	(6,238)	–	–
Forfeited in year	–	(7,353)	–	–	–
Outstanding 31 December 2014	625,328	–	327,760	3,120,900	1,773,880
Of which exercisable	625,328	–	–	–	–

	Ordinary Shares			A and B Ordinary Shares
	Long-term incentive plan[2]	Deferred bonus share plan[2]	IPO incentive scheme[2,4]	Growth shares[5]
Shares in existence at 1 January 2014	–	–	–	1,123,407
Conversion of A and B Ordinary Shares	–	–	–	(1,123,407)
Crystallisation of IPO incentive scheme	–	–	1,661,631	–
Granted in year	105,448	14,918	–	–
Exercised or vested in year	(105,448)	–	(996,973)	–
Outstanding 31 December 2014	–	14,918	664,658	–
Of which exercisable	–	–	–	–

1 This scheme was set up for the previous Chairman, Sir David Clementi. All share options granted under the scheme had vested as at 31 December 2014. During 2014, 32,912 share options were exercised for a weighted-average exercise price of £2.15. The weighted-average exercise price for options outstanding at 1 January 2014 and 31 December 2014 was £2.15. The options outstanding will expire 10 years from the date of listing if not exercised.

2 Awards have vesting conditions.

3 Immediately prior to listing, there was a reorganisation of share capital.

4 The IPO incentive scheme was awarded as a percentage of the listing value, which is then converted to a number of shares based on the listing price. On listing 1,661,631 Ordinary Shares were awarded.

5 Growth shares were A and B Ordinary Shares. The return on these shares on listing was calculated as set out in the Company's Articles of Association. A Ordinary Shares were converted into 38,055 Ordinary Shares and 1,064,927 Deferred Shares. B Ordinary Shares were converted into 9,192 Ordinary Shares and 92,936 Deferred Shares. The Deferred Shares created on the conversion of the A and B Ordinary Shares were then cancelled.

Notes to the consolidated financial statements

Note 8: Allowance for impairment losses on loans and receivables

	On secured loans £m	On unsecured loans £m	Total £m
At 1 January 2014	7.6	27.1	34.7
Advances written off	(1.2)	(27.6)	(28.8)
Gross charge to the income statement	1.2	23.5	24.7
At 31 December 2014	7.6	23.0	30.6
Advances written off	**(1.9)**	**(26.0)**	**(27.9)**
Gross charge to the income statement	**3.0**	**34.2**	**37.2**
As at 31 December 2015	**8.7**	**31.2**	**39.9**

Of the total allowance in respect of loans and advances to customers, £38.8 million (2014: £27.6 million) was assessed on a collective basis.

During the year, sales of credit card receivables which had previously been written-off resulted in net recoveries of £6.9 million (2014: £8.9 million). The full amount of the proceeds have been recognised as a gain and the net charge to the income statement is summarised below.

	2015 £m	2014 £m
Gross charge to the income statement	**37.2**	24.7
Debt sale recoveries	**(6.9)**	(8.9)
Net charge to the income statement	**30.3**	15.8

Note 9: Taxation

(A) Analysis of the tax charge for the year

	2015 £m	2014 £m
UK corporation tax		
Current tax on profit for the year	**(13.6)**	(0.7)
Adjustments in respect of prior years	**–**	(2.3)
Current tax charge to the income statement	**(13.6)**	(3.0)
Deferred tax (refer note 22)		
Origination and reversal of temporary differences	**(15.0)**	(16.5)
Adjustments in respect of prior years	**(0.7)**	(6.0)
Reduction in UK corporation tax rate	**2.5**	0.2
Deferred tax charge to the income statement	**(13.2)**	(22.3)
Tax charge	**(26.8)**	(25.3)

Notes to the consolidated financial statements

Note 9: Taxation (continued)

Analysis of tax charge recognised in Other Comprehensive Income:

	2015 £m	2014 £m
Current tax		
Available-for-sale financial assets	**2.1**	(1.3)
Deferred tax		
Available-for-sale financial assets	**(0.9)**	–
Cash flow hedge	**1.6**	2.5
Total credit	**2.8**	1.2

(B) Factors affecting the tax charge for the year

A reconciliation of the charge that would result from applying the standard UK corporation tax rate to the profit before tax to the actual tax charge for the year is given below:

	2015 £m	2014 £m
Profit before tax	**138.0**	34.0
Tax charge at effective corporation tax rate of 20.25% (2014: 21.5%)	**(27.9)**	(7.3)
Factors affecting charge:		
Disallowed items	**(1.5)**	(11.6)
Non-taxable income	**0.8**	1.1
UK corporation tax rate change	**2.5**	0.2
Adjustments in respect of previous years	**(0.7)**	(8.3)
Gains covered by the substantial shareholding exemption	**–**	1.0
Other items	**–**	(0.4)
Total tax charge	**(26.8)**	(25.3)

The Group has been engaged in discussion with HM Revenue and Customs (HMRC) regarding the tax treatment of certain commercial funding transactions that were entered into during 2009 involving Virgin Money Cards Limited (since renamed Sapphire Cards Limited), which is no longer part of the Group. Tax charges of £8.8 million in relation to the settlement of the HMRC enquiry were reflected within the 2014 Adjustments in respect of prior periods. This includes an anticipated benefit from the surrender of up to £62.9 million of tax losses by the Virgin Group for an expected payment in the region of £15.5 million.

The Finance Act 2013 (the Act) was substantively enacted on 2 July 2013. The Act reduced the main rate of corporation tax to 21% with effect from 1 April 2014 and 20% with effect from 1 April 2015. The Finance (No. 2) Act 2015 was substantively enacted on 26 October 2015. This reduced the main rate of corporation tax further to 19% with effect from 1 April 2017 and to 18% with effect from 1 April 2020.

A bank corporation tax surcharge of 8%, effective from 1 January 2016, was enacted in November 2015. Whilst the surcharge will not apply to the banking profits of the Group's operating bank subsidiary, Virgin Money plc until 2016, it has been necessary to rebase deferred tax assets and liabilities, where relevant, to ensure that such assets and liabilities continue to be held on the balance sheet using the rate at which they are expected to reverse in the future. As at 31 December 2015, this rate uplift has been reflected for Virgin Money plc's deferred tax assets and liabilities, except in relation to brought forward trading losses which fall outside of the surcharge rules. The most material element of the rate change impact of £2.5 million, set out above, is accounted for by this surcharge rate uplift.

Notes to the consolidated financial statements

Note 10: Earnings per share

The Group presents basic and diluted earnings per share (EPS) data in relation to the ordinary shares of the Company.

Earnings per share

	2015 £m	2014 £m
Profit attributable to equity shareholders – basic and diluted	**111.2**	8.7
Distributions to Non-core Tier 1 noteholders and Additional Tier 1 security holders (net of group relief)	**(10.0)**	(10.3)
Profit/(loss) attributable to equity holders for the purposes of basic and diluted EPS	**101.2**	(1.6)

	2015 Number of shares (million)	2014 Number of shares (million)
Weighted-average number of ordinary shares in issue – basic	**441.0**	391.3
Adjustment for share options and awards	**4.7**	0.3
Weighted-average number of ordinary shares in issue – diluted	**445.7**	391.6
Basic earnings per share (pence)	**22.9**	(0.4)
Diluted earnings per share (pence)	**22.7**	(0.4)

Basic earnings per share has been calculated after deducting 1.8 million (2014: 1.6 million) ordinary shares representing the Group's holdings of own shares in respect of employee share schemes.

Of the total number of employee share options and share awards at 31 December 2015 none were anti-dilutive (2014: 6.6 million).

Note 11: Dividends

The Directors have recommended for approval at the 2016 AGM the payment of a final dividend in respect of the year ended 31 December 2015 of 3.1p per ordinary share, amounting to £13.7 million. If approved, this final dividend will be paid on 25 May 2016 to shareholders on the register at close of business on 15 April 2016. The financial statements for the year ended 31 December 2015 do not reflect this final dividend, which will be accounted for in shareholders' equity as an appropriation of retained profits in the year ending 31 December 2016.

The 2015 interim dividend of 1.4p per ordinary share, amounting to £6.2 million, was paid in October 2015 and has been deducted from retained profits.

Under the trust deed of the Employee Benefit Trust (EBT), a standing waiver is in force in respect of any dividends declared on shares held by the EBT.

There were no dividends declared or paid in the year ending 31 December 2014.

Notes to the consolidated financial statements

Note 12: Analysis of financial assets and financial liabilities by measurement basis

	Held at amortised cost £m	Loans and receivables £m	Available-for-sale securities £m	Derivatives not designated as hedging instruments £m	Derivatives designated as hedging instruments		Total £m
					Fair value hedges £m	Cash flow hedges £m	
As at 31 December 2015							
Financial assets							
Cash and balances at central banks	–	888.6	–	–	–	–	888.6
Derivative financial instruments	–	–	–	18.3	63.5	0.5	82.3
Loans and receivables:							
– Loans and advances to banks	–	614.5	–	–	–	–	614.5
– Loans and advances to customers	–	27,109.0	–	–	–	–	27,109.0
– Debt securities	–	1.1	–	–	–	–	1.1
Available-for-sale financial assets	–	–	1,296.9	–	–	–	1,296.9
Other assets – trade debtors and accrued income	–	14.6	–	–	–	–	14.6
Total financial assets	–	28,627.8	1,296.9	18.3	63.5	0.5	30,007.0
Non financial assets							222.0
Total assets							30,229.0
Financial liabilities							
Deposits from banks	1,298.7	–	–	–	–	–	1,298.7
Customer deposits	25,144.9	–	–	–	–	–	25,144.9
Derivative financial instruments	–	–	–	15.4	139.6	1.0	156.0
Debt securities in issue	2,039.4	–	–	–	–	–	2,039.4
Other liabilities – trade creditors and accrued interest	155.1	–	–	–	–	–	155.1
Total financial liabilities	28,638.1	–	–	15.4	139.6	1.0	28,794.1
Non financial liabilities							94.6
Total liabilities							28,888.7
Equity							1,340.3
Total liabilities and equity							30,229.0

Notes to the consolidated financial statements

Note 12: Analysis of financial assets and financial liabilities by measurement basis (continued)

	Held at amortised cost £m	Loans and receivables £m	Available-for-sale securities £m	Derivatives not designated as hedging instruments £m	Derivatives designated as hedging instruments Fair value hedges £m	Derivatives designated as hedging instruments Cash flow hedges £m	Total £m
As at 31 December 2014							
Financial assets							
Cash and balances at central banks	–	851.3	–	–	–	–	851.3
Derivative financial instruments	–	–	–	25.9	75.3	–	101.2
Loans and receivables:							
– Loans and advances to banks	–	720.5	–	–	–	–	720.5
– Loans and advances to customers	–	23,093.1	–	–	–	–	23,093.1
– Debt securities	–	8.6	–	–	–	–	8.6
Available-for-sale financial assets	–	–	1,539.6	–	–	–	1,539.6
Other assets – trade debtors and accrued income	–	17.5	–	–	–	–	17.5
Total financial assets	–	24,691.0	1,539.6	25.9	75.3	–	26,331.8
Non financial assets							205.0
Total assets							26,536.8
Financial liabilities							
Deposits from banks	846.7	–	–	–	–	–	846.7
Customer deposits	22,365.7	–	–	–	–	–	22,365.7
Derivative financial instruments	–	–	–	22.0	203.7	2.5	228.2
Debt securities in issue	1,594.1	–	–	–	–	–	1,594.1
Other liabilities – trade creditors and accrued interest	165.2	–	–	–	–	–	165.2
Total financial liabilities	24,971.7	–	–	22.0	203.7	2.5	25,199.9
Non financial liabilities							93.1
Total liabilities							25,293.0
Equity							1,243.8
Total liabilities and equity							26,536.8

Notes to the consolidated financial statements

Note 13: Derivative financial instruments

	2015			2014		
	Contract/ notional amount £m	**Asset fair value £m**	**Liability fair value £m**	Contract/ notional amount £m	Asset fair value £m	Liability fair value £m
Derivatives in accounting hedge relationships						
Derivatives designated as fair value hedges:						
Interest rate swaps	**23,421.6**	**63.5**	**(139.6)**	22,160.5	74.4	(203.7)
Cross currency interest rate swaps	**–**	**–**	**–**	21.8	0.9	–
	23,421.6	**63.5**	**(139.6)**	22,182.3	75.3	(203.7)
Derivatives designated as cash flow hedges:						
Interest rate swaps	**369.7**	**0.5**	**(1.0)**	811.8	–	(2.5)
Total derivative assets/(liabilities) – in accounting hedge relationships	**23,791.3**	**64.0**	**(140.6)**	22,994.1	75.3	(206.2)
Derivatives in economic hedging relationships but not in accounting hedge relationships						
Interest rate contracts:						
Interest rate swaps	**3,651.4**	**16.8**	**(15.4)**	3,345.9	24.8	(21.8)
Options:						
Equity FTSE 100 options	**–**	**1.5**	**–**	–	1.1	(0.2)
Total derivative assets/(liabilities) – in economic hedging relationship but not in accounting hedge relationships	**3,651.4**	**18.3**	**(15.4)**	3,345.9	25.9	(22.0)
Total recognised derivative assets/(liabilities)	**27,442.7**	**82.3**	**(156.0)**	26,340.0	101.2	(228.2)

The principal amount of the derivative contracts does not represent the Group's real exposure to credit risk which is limited to the current cost of replacing contracts with a positive value to the Group should the counterparty default. To reduce credit risk the Group uses a variety of credit enhancement techniques such as netting and collateralisation, where security is provided against the exposure. Further details are provided in the Risk Management Report.

Hedged cash flows

For designated cash flow hedges the following table shows when the Group's hedged cash flows are expected to occur and when they will impact income:

	2015 £m	2014 £m
Within one year	**(5.5)**	(2.9)
In one to five years	**(9.8)**	(5.9)
Total	**(15.3)**	(8.8)

Notes to the consolidated financial statements

Note 13: Derivative financial instruments (continued)

Gains/(losses) from derivatives and hedge accounting

	2015 £m	2014 £m
Gain/(loss) from fair value hedge accounting[1]:		
Derivatives designated as fair value hedges	**53.7**	(156.3)
Fair value movement attributable to hedged risk	**(50.7)**	155.1
	3.0	(1.2)
Loss from cash flow hedges	**(5.1)**	(2.7)
Fair value gains from other derivatives[2]	**1.7**	4.0
(Loss)/gain from derivatives and hedge accounting	**(0.4)**	0.1

1 Gains or losses from fair value hedges can arise where there is an IFRS hedge accounting relationship in place and either:
– the fair value of the derivative was not exactly offset by the change in fair value attributable to the hedged risk; or
– the derivative was designated in or dedesignated from the IFRS hedge accounting relationship and in the following months leads to amortisation of existing balance sheet positions.

2 Other derivatives are those used for economic hedging but which are not in an IAS 39 hedge accounting relationship.

Note 14: Loans and advances to banks

Loans and advances to banks comprise:

	2015 £m	2014 £m
Balances within securitisation vehicles	**384.3**	447.9
Money market placements with banks	**97.1**	120.8
Other lending to banks	**133.1**	151.8
Total	**614.5**	720.5

Note 15: Loans and advances to customers

Loans and advances to customers comprise:

	2015 £m	2014 £m
Advances secured on residential property not subject to securitisation	**17,389.9**	15,631.2
Advances secured on residential property subject to securitisation	**3,670.4**	3,128.3
	21,060.3	18,759.5
Residential buy-to-let loans not subject to securitisation	**4,401.9**	3,135.6
Total loans and advances to customers secured on residential property	**25,462.2**	21,895.1
Unsecured receivables not subject to securitisation	**1,610.0**	1,121.3
Total loans and advances to customers before allowance for impairment losses	**27,072.2**	23,016.4
Impairment allowance (refer note 8)	**(39.9)**	(30.6)
Total loans and advances to customers excluding portfolio hedging	**27,032.3**	22,985.8
Fair value of portfolio hedging	**76.7**	107.3
Total loans and advances to customers	**27,109.0**	23,093.1

The fair value of portfolio hedging represents an accounting adjustment which offsets the fair value movement on the related derivatives. Such relationships are established to protect the Group from interest rate risk on fixed rate products. See the Risk Management Report for further details.

For collateral held in respect of the values included in the table above, refer to the Risk Management Report.

Notes to the consolidated financial statements

Note 16: Available-for-sale financial assets

	2015 £m	2014 £m
At 1 January	**1,539.6**	1,679.2
Additions	**659.2**	567.6
Disposals (sales and redemptions)	**(859.9)**	(789.1)
Reclassification of equity investments[1]	**1.3**	–
Exchange differences	**(0.7)**	(1.3)
Net gains on changes in fair value	**(42.6)**	83.2
At 31 December	**1,296.9**	1,539.6

1 Represents investments in unquoted equity securities relating to the Group's participation in banking and credit card operations, previously recognised within Other assets.

Gains on sale of available-for-sale securities amounted to £8.8 million (2014: £7.5 million).

Analysis of the composition of debt securities categorised as available-for-sale financial assets is set out in the Risk Management Report. All assets have been individually assessed for impairment and following this assessment no write down of assets was required.

For amounts included above which are subject to repurchase agreements refer to note 17.

Note 17: Collateral pledged and received

The Group receives and accepts collateral in the form of cash and marketable securities in respect of the following transactions:

- derivatives;
- sale and repurchase and reverse sale and repurchase agreements; and
- securities lending and borrowing.

Collateral in respect of derivatives is subject to the standard industry terms of ISDA Credit Support Annex. This means that securities received or given as collateral can be pledged or sold during the term of the transaction but must be returned on maturity of the transaction. The terms also give each counterparty the right to terminate the related transactions upon the counterparty's failure to post collateral.

At 31 December 2015 cash collateral of £94.6 million (2014: £121.8 million) had been pledged by the Group and £23.8 million (2014: £11.4 million) has been received as cash collateral by the Group.

At 31 December 2015 available-for-sale financial assets of £nil (2014: £291.4 million) are pledged as collateral in respect of sale and repurchase agreements under terms that are usual and customary for such activities.

At 31 December 2015 loans and advances of £755.0 million (2014: £723.9 million) are pledged as collateral in respect of sale and repurchase agreements under terms that are usual and customary for such activities.

The value of collateral pledged in respect of repurchase agreements that was transferred, accounted for as secured borrowings, where the transfer is permitted by contract or custom to repledge collateral was £nil (2014: £274.3 million).

Notes to the consolidated financial statements

Note 18: Securitisation

Assets and liabilities of the SPVs included in these consolidated financial statements comprise:

	2015 £m	2014 £m
Assets		
Loans and advances to customers	**3,670.4**	3,128.3
Loans and advances to banks	**384.3**	447.9
Other assets	**0.3**	0.2
Total assets	**4,055.0**	3,576.4
Liabilities		
Debt securities in issue	**1,741.9**	1,594.1
Deposits by banks	**13.2**	0.1
Derivative financial instruments	**–**	0.1
Other liabilities	**3.1**	4.9
Total liabilities	**1,758.2**	1,599.2

The following table sets out the carrying amount of financial assets that did not qualify for derecognition and their associated liabilities. Where relevant, the table also sets out the net position of the fair value of financial assets where the counterparty to the associated liabilities has recourse only to the financial assets.

	2015 £m	2014 £m
Carrying amount of transferred assets	**3,670.4**	3,128.3
Fair value of transferred assets	**3,728.4**	3,197.4
Carrying amount of associated liabilities	**1,741.9**	1,594.1
Fair value of associated liabilities	**1,740.0**	1,599.6

There were no transactions in the year where the Group transferred financial assets that should have been derecognised in their entirety.

Note 19: Acquisitions and disposals

Disposal of CHT (2014)

The disposal of CHT was completed on 30 November 2014. A gain on disposal of £4.5 million was recognised on that date by the Group.

Purchase of credit card portfolio (2014)

From the point of acquisition of the credit card book from MBNA on 18 January 2013, until 30 November 2014, MBNA agreed to underwrite and administer new Virgin Money branded credit cards on a commission basis. On 30 November 2014, the Group completed an agreement to purchase the assets originated during this period. The portfolio was purchased for a consideration of £362.7 million. The fair value of the assets purchased was £354.5 million (a premium of £8.2 million). This included credit cards that had previously been charged-off. The premium will be unwound over the life of the purchased assets.

The acquisition was determined to be an asset purchase as the assets were purchased without staff contracts or processes or other aspects of the business being transferred to them.

Notes to the consolidated financial statements

Note 20: Intangible assets

Intangible assets comprise:

	Core deposit intangible £m	Goodwill £m	Software £m	Core banking platform £m	Total £m
Cost:					
Cost at 1 January 2014	4.8	4.6	68.1	6.9	84.4
Additions	–	–	13.9	13.0	26.9
Disposals	–	(4.6)	–	–	(4.6)
Cost at 31 December 2014	4.8	–	82.0	19.9	106.7
Additions	**–**	**–**	**27.9**	**1.6**	**29.5**
Disposals	**–**	**–**	**(24.8)**	**–**	**(24.8)**
At 31 December 2015	**4.8**	**–**	**85.1**	**21.5**	**111.4**
Accumulated amortisation:					
Accumulated amortisation at 1 January 2014	2.7	4.6	51.1	–	58.4
Charge for the year	1.0	–	5.8	–	6.8
Disposals	–	(4.6)	–	–	(4.6)
Accumulated amortisation at 31 December 2014	3.7	–	56.9	–	60.6
Charge for the year	**(0.3)**	**–**	**8.6**	**2.9**	**11.2**
Disposals	**–**	**–**	**(24.8)**	**–**	**(24.8)**
At 31 December 2015	**3.4**	**–**	**40.7**	**2.9**	**47.0**
Balance sheet amount at 31 December 2015	**1.4**	**–**	**44.4**	**18.6**	**64.4**
Balance sheet amount at 31 December 2014	1.1	–	25.1	19.9	46.1

Additions during the year relate to software and core banking platform intangible assets. Software additions primarily relate to the purchase of new office software for employee workstations, as well as further development of the Group's digital banking channel.

Notes to the consolidated financial statements

Note 21: Tangible fixed assets

Tangible fixed assets comprise:

	Land and buildings £m	Plant, equipment fixtures, fittings and vehicles £m	Total £m
Cost:			
Cost at 1 January 2014	59.1	35.5	94.6
Additions	4.2	6.4	10.6
Disposals	(2.1)	(0.3)	(2.4)
Cost at 31 December 2014	61.2	41.6	102.8
Additions	**2.1**	**8.1**	**10.2**
Disposals	**–**	**(10.2)**	**(10.2)**
At 31 December 2015	**63.3**	**39.5**	**102.8**
Accumulated depreciation and impairment:			
Accumulated depreciation and impairment at 1 January 2014	6.5	16.9	23.4
Depreciation charge for the year	2.1	5.9	8.0
Disposals	(1.3)	(0.2)	(1.5)
Accumulated depreciation and impairment at 31 December 2014	7.3	22.6	29.9
Depreciation charge for the year	**2.2**	**6.2**	**8.4**
Disposals	**–**	**(10.1)**	**(10.1)**
At 31 December 2015	**9.5**	**18.7**	**28.2**
Balance sheet amount at 31 December 2015	**53.8**	**20.8**	**74.6**
Balance sheet amount at 31 December 2014	53.9	19.0	72.9

Notes to the consolidated financial statements

Note 22: Deferred tax assets

Deferred tax assets and liabilities comprise:

	2015 £m	2014 £m
Deferred tax assets/(liabilities):		
Accelerated capital allowances	**15.1**	7.1
Cash flow hedge reserve	**3.8**	2.2
Change in accounting basis on adoption of IFRS	**(4.8)**	(3.0)
Tax losses carried forward	**18.0**	38.1
Other temporary differences	**4.3**	4.4
Fair value adjustments on acquisition of Northern Rock	**1.6**	1.4
Total deferred tax assets	**38.0**	50.2

The Group has not recognised deferred tax assets in respect of gross unused tax losses of £31.2 million (2014: £28.8 million).

The movement in the net deferred tax balance is as follows:

	2015 £m	2014 £m
At 1 January	**50.2**	70.0
Income statement (charge)/credit (refer note 9):		
Accelerated capital allowances	**8.0**	(1.5)
Tax losses carried forward	**(20.1)**	(24.1)
Other temporary differences	**(1.1)**	3.3
	(13.2)	(22.3)
Amounts credited/(charged) to equity:		
Available-for-sale financial assets	**(0.9)**	–
Cash flow hedges	**1.6**	2.5
Adjustments relating to share based payments	**0.3**	–
	1.0	2.5
At 31 December	**38.0**	50.2

Note 23: Other assets

Other assets comprise:

	2015 £m	2014 £m
Trade debtors	**9.7**	12.6
Prepayments and accrued income	**22.4**	16.8
Other	**27.5**	23.9
Total other assets	**59.6**	53.3

Notes to the consolidated financial statements

Note 24: Deposits from banks

Deposits from banks comprise:

	2015 £m	2014 £m
Liabilities in respect of securities sold under repurchase agreements	**1,274.9**	835.3
Other deposits from banks	**23.8**	11.4
Total deposits from banks	**1,298.7**	846.7

Note 25: Customer deposits

Customer deposits comprise:

	2015 £m	2014 £m
Savings and investment accounts	**24,914.6**	22,164.1
Personal current accounts	**230.3**	201.6
Total customer deposits	**25,144.9**	22,365.7

Note 26: Debt securities in issue

Debt securities in issue comprise:

	Secured £m	Unsecured £m	Total £m
At 1 January 2014	1,469.8	–	1,469.8
Repayments	(874.1)	–	(874.1)
Issues	1,000.0	–	1,000.0
Other movements	(1.6)	–	(1.6)
At 31 December 2014	1,594.1	–	1,594.1
Repayments	**(601.9)**	**–**	**(601.9)**
Issues	**750.0**	**298.9**	**1,048.9**
Other movements	**(0.3)**	**(1.4)**	**(1.7)**
At 31 December 2015	**1,741.9**	**297.5**	**2,039.4**

Other movements comprise accrued interest, unamortised issue costs or hedge accounting adjustments.

On 16 April 2015, the Group issued 5 year Medium Term Notes with a nominal value of £300 million at a coupon of 2.25% per annum. The notes were issued as part of the Group's recently launched £3 billion Global Medium Term Note programme, which was established to diversify the Group's wholesale funding base further.

On 8 June 2015, the Group raised £750 million from institutional investors through the issuance of Residential Mortgage Backed Securities in the Gosforth Funding 2015-1 transaction.

Notes to the consolidated financial statements

Note 27: Provisions

The movement in provisions was as follows:

	FSCS £m	Other £m	Total £m
At 1 January 2015	**8.7**	**0.6**	**9.3**
Provisions applied	**(14.6)**	**(0.2)**	**(14.8)**
Charge for the year	**12.5**	**1.4**	**13.9**
At 31 December 2015	**6.6**	**1.8**	**8.4**

The Financial Services Compensation Scheme (FSCS) is the UK's statutory fund of last resort for customers of authorised financial services firms and pays compensation if a firm is unable to pay claims against it. The FSCS has borrowed from HM Treasury to fund the compensation costs associated with institutions that failed in 2008 and will receive the receipts from asset sales, surplus cash flows and other recoveries from these institutions in the future. The FSCS meets its obligations by raising management expense and compensation levies. These include amounts to cover the interest on its borrowings and on-going management expenses. Each deposit taking institution contributes in proportion to its share of total protected deposits.

The FSCS can only raise a levy within its scheme year (which commences 1 April) and under IFRIC 21 'Levies' the Group recognises its FSCS provision in the scheme year itself.

Note 28: Other liabilities

Other liabilities comprise:

	2015 £m	2014 £m
Trade creditors	**24.0**	26.3
Deferred income	**5.0**	4.8
Other creditors and accruals	**206.0**	215.6
Current tax liabilities	**6.3**	2.3
Total other liabilities	**241.3**	249.0

Deferred income represents income advanced from partners that will be recognised in future periods.

Accrued interest included within 'Other creditors and accruals' primarily represents interest which has accrued on retail funds and deposits.

The Group's exposure to liquidity risk related to trade and other payables is disclosed in the Risk Management Report.

Notes to the consolidated financial statements

Note 29: Share capital and share premium

Share capital and share premium

	2015 £m	2014 £m
Share capital	**0.1**	0.1
Share premium		
At 1 January	**654.5**	509.2
Premium on shares issued in the year	–	149.9
Ordinary Share issue costs charged directly to equity	–	(4.6)
As at 31 December	**654.5**	654.5
At 31 December	**654.6**	654.6

Issued and fully paid share capital

	2015 Number of shares	2014 Number of shares
Ordinary Shares of £0.0001 each		
At 1 January	**441,933,180**	38,742,729
Share conversion	–	47,247
Subdivision of shares	–	349,109,784
Issued during year	**1,778,278**	53,003,534
Issued under employee share schemes	–	1,029,886
At 31 December	**443,711,458**	441,933,180
Deferred Shares of £0.001 each		
At 1 January	**10,052,161**	731,113
Issued during year	–	9,321,048
Share conversion	–	1,157,863
Shares cancellation	–	(1,157,863)
At 31 December	**10,052,161**	10,052,161

During the year, the Company issued 1,778,278 Ordinary Shares in advance of the vesting of awards granted under the IPO share award and the IPO incentive scheme.

The total number of Ordinary Shares in issue at 31 December 2015 was 443,711,458 with a nominal value of £0.0001, amounting to £44,371 (2014: 441,933,180 Ordinary Shares with a nominal value of £0.0001, amounting to £44,193). The total number of Deferred Shares in issue at 31 December 2015 was 10,052,161, with a nominal value of £0.001, amounting to £10,052 (2014: 10,052,161 Deferred Shares with a nominal value of £0.001, amounting to £10,052).

Previously the Company had issued A Ordinary Shares and B Ordinary Shares, neither of which carried any voting rights. During 2014 all of the 1,102,982 A Ordinary Shares (1 January 2014: 1,102,982) and 102,128 B Ordinary Shares (1 January 2014: Nil) each with a nominal value of £0.001 per share, were converted into a combination of Ordinary Shares and Deferred Shares (refer note 7). The conversion was based on the calculation and hurdle rate specified in the Articles of Association of the Company.

The following describes the rights attaching to each share class at 31 December 2015:

Ordinary Shares

The holders of Ordinary Shares are entitled to one vote per share at meetings of the Group. All Ordinary Shares in issue in the Company rank equally and carry the same voting rights and the same rights to receive dividends and other distributions declared or paid by the Company.

Notes to the consolidated financial statements

Note 29: Share capital and share premium (continued)

Deferred Shares

As set out in the Articles of Association adopted on listing (and pursuant to the provisions of the Companies Act in respect of shares held in own shares), the Deferred Shares have no voting or dividend rights and, on a return of capital on a winding up, have no valuable economic rights. No application has been made or is currently intended to be made for the Deferred Shares to be admitted to the Official List or to trade on the London Stock Exchange or any other investment exchange.

The Deferred Shares are held in treasury. This is to ensure that the aggregate nominal value of the Company's share capital will be not less than £50,000, which is the minimum level of nominal share capital required by the Companies Act for a company to be established as a public limited company.

Note 30: Other equity instruments

The Company issued Fixed Rate Resettable Additional Tier 1 (AT1) securities of £160.0 million on the Luxembourg Stock Exchange on 31 July 2014. This issue is treated as an equity instrument in accordance with IAS 32 'Financial Instruments: Presentation' with the proceeds included in equity, net of transaction costs of £3.5 million. Dividends and other returns to equity holders are treated as a deduction from equity. The principal terms of the securities are described below:

- the securities constitute direct, unsecured and subordinated obligations of the Company and rank pari passu with holders of other Tier 1 instruments and the holders of that class or classes of preference shares but rank junior to the claims of senior creditors;
- the securities bear a fixed rate of interest from the issue date of 7.875% until the first reset date on the 5th anniversary;
- interest on the securities will be due and payable only at the sole discretion of the Company, and the Company has sole and absolute discretion at all times and for any reason to cancel (in whole or in part) any interest payment that would otherwise be payable on any interest payment date;
- the securities are undated and are redeemable, at the option of the Company, all (but not part) on the first reset date or any reset date thereafter. In addition, the AT1 securities are redeemable, at the option of the Company, in whole for certain regulatory or tax reasons. Any optional redemption requires the prior consent of the PRA; and
- all AT1 securities will be converted into Ordinary Shares of the Company, at a pre-determined price, should the Common Equity Tier 1 ratio of the Group fall below 7.0% as specified in the terms.

Notes to the consolidated financial statements

Note 31: Other reserves

Other reserves comprise:

	2015 £m	2014 £m
Available-for-sale reserve		
At 1 January	**7.0**	6.5
Net (losses)/gains from changes in fair value	**(0.8)**	86.9
Net gains on disposal transferred to net income	**(33.6)**	(10.3)
Amounts transferred to net income due to hedge accounting	**25.9**	(74.8)
Taxation	**1.2**	(1.3)
At 31 December	**(0.3)**	7.0

	2015 £m	2014 £m
Cash flow hedge reserve		
At 1 January	**(8.8)**	0.2
Amounts recognised in equity	**(13.2)**	(14.1)
Amounts transferred to income statement	**5.1**	2.6
Deferred tax	**1.6**	2.5
At 31 December	**(15.3)**	(8.8)

Notes to the consolidated financial statements

Note 32: Retained earnings

Retained earnings comprise:

	2015 £m	2014 £m
At 1 January	**434.5**	419.0
Profit for the year	**111.2**	8.7
Dividends and distributions to Tier 1 security holders (net of tax)	**(16.2)**	(10.3)
Purchase of own shares	**(5.0)**	–
Share based payments (including deferred tax)	**20.3**	17.1
As at 31 December	**544.8**	434.5

Employee Benefit Trust (EBT)

Retained earnings are stated after deducting £2.9 million (2014: £2.1 million) representing 1,815,387 (2014: 1,561,013) own shares held in an EBT.

As part of an arrangement to allow holders of certain shares in the Company an opportunity to access some of the value increase in the Group since the original grant date, the Company established an EBT in 2011. The Company funded the EBT by means of a cash loan and is therefore considered to be the sponsoring entity. The EBT purchased shares in the Company using the cash loan which is accounted for as a purchase of own shares by the Company. The investment in own shares at 31 December 2015 is £2.9 million (2014: £2.1 million). The market value of the shares held in the EBT at 31 December 2015 was £6.9 million.

Note 33: Contingent liabilities and commitments

Contingent liabilities

The Board was not aware of any significant contingent liabilities as at 31 December 2015 (31 December 2014: none).

The Company is, from time to time and in the normal course of business, subject to a variety of legal or regulatory claims, actions or proceedings. When such circumstances arise, the Board considers the likelihood of a material outflow of economic resources and provides for its best estimate of costs where an outflow of economic resources is considered probable. While there can be no assurances, the Directors believe, based on information currently available to them, that the likelihood of material outflows from such matters is remote.

The Board does not expect the ultimate resolution of any other threatened or actual legal proceedings to have a significant adverse effect on the financial position of the Group.

Notes to the consolidated financial statements

Note 33: Contingent liabilities and commitments (continued)

Loan commitments

Contractual amounts to which the Group is committed for extension of credit to customers.

	2015 £m	2014 £m
Not later than 1 year	**3,958.7**	3,100.2
Later than one year and not later than 5 years	**–**	–
Later than 5 years	**521.1**	594.0
Total loan commitments	**4,479.8**	3,694.2

Operating lease commitments – land and buildings

Minimum future lease payments under non-cancellable operating leases.

	2015 £m	2014 £m
Not later than 1 year	**7.2**	7.1
Later than one year and not later than 5 years	**25.2**	24.3
Later than 5 years	**24.1**	23.3
Total operating lease commitments – land and buildings	**56.5**	54.7

Operating lease commitments – other operating leases

Minimum future lease payments under non-cancellable operating leases.

	2015 £m	2014 £m
Not later than 1 year	**4.6**	4.6
Later than one year and not later than 5 years	**9.2**	13.8
Later than 5 years	**–**	–
Total operating lease commitments – other operating leases	**13.8**	18.4

Capital commitments

Capital commitments for the acquisition of buildings and equipment.

	2015 £m	2014 £m
Not later than 1 year	**2.9**	5.7
Later than one year and not later than 5 years	**–**	–
Later than 5 years	**–**	–
Total capital commitments	**2.9**	5.7

Notes to the consolidated financial statements

Note 34: Fair value of financial assets and liabilities

Fair value of financial assets and liabilities recognised at cost

The following table summarises the fair values of those financial assets and liabilities not presented on the Group's balance sheet at their fair value, by the level in the fair value hierarchy into which each fair value measurement is categorised. The accounting policy in note 1.9 (j) sets out the key principles for estimating the fair values of financial instruments.

	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m	Total carrying value £m
At 31 December 2015					
Cash and balances at central banks	**–**	**888.6**	**–**	**888.6**	**888.6**
Loans and advances to banks	**–**	**614.5**	**–**	**614.5**	**614.5**
Loans and advances to customers[1]	**–**	**–**	**27,243.2**	**27,243.2**	**27,109.0**
Debt securities classified as loans and receivables	**1.2**	**–**	**–**	**1.2**	**1.1**
Available-for-sale financial assets	**–**	**–**	**1.3**	**1.3**	**1.3**
Other assets – trade debtors and accrued income	**–**	**14.6**	**–**	**14.6**	**14.6**
Total financial assets at fair value	**1.2**	**1,517.7**	**27,244.5**	**28,763.4**	**28,629.1**
Deposits from banks	**–**	**1,298.7**	**–**	**1,298.7**	**1,298.7**
Customer deposits	**–**	**25,162.5**	**–**	**25,162.5**	**25,144.9**
Debt securities in issue	**2,032.1**	**–**	**–**	**2,032.1**	**2,039.4**
Other liabilities – trade payables and accrued interest	**–**	**155.1**	**–**	**155.1**	**155.1**
Total financial liabilities at fair value	**2,032.1**	**26,616.3**	**–**	**28,648.4**	**28,638.1**

1 Amounts shown in respect of loans and advances to customers includes fair value adjustments of portfolio hedging.

	Level 1 £m	Level 2 £m	Level 3 £m	Total fair value £m	Total carrying value £m
At 31 December 2014					
Cash and balances at central banks	–	851.3	–	851.3	851.3
Loans and advances to banks	–	720.5	–	720.5	720.5
Loans and advances to customers[1]	–	–	23,197.2	23,197.2	23,093.1
Debt securities classified as loans and receivables	10.0	–	–	10.0	8.6
Other assets – trade debtors and accrued income	–	17.5	–	17.5	17.5
Total financial assets at fair value	10.0	1,589.3	23,197.2	24,796.5	24,691.0
Deposits from banks	–	846.7	–	846.7	846.7
Customer deposits	–	22,424.3	–	22,424.3	22,365.7
Debt securities in issue	1,599.6	–	–	1,599.6	1,594.1
Other liabilities – trade creditors and accrued interest	–	165.2	–	165.2	165.2
Total financial liabilities at fair value	1,599.6	23,436.2	–	25,035.8	24,971.7

1 Amounts shown in respect of loans and advances to customers includes fair value adjustments of portfolio hedging.

Notes to the consolidated financial statements

Note 34: Fair value of financial assets and liabilities (continued)

Fair value hierarchy

The table above summarises the carrying value and fair value of assets and liabilities held on the balance sheet. There are three levels to the hierarchy as follows:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets and liabilities.

Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, whether directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3 – Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Valuation methods for calculations of fair values in the table above are set out below:

Cash and balances at central banks

Fair value approximates to carrying value because cash and balances at central banks have minimal credit losses and are either short-term in nature or reprice frequently.

Loans and advances to banks

Fair value was estimated by using discounted cash flows applying either market rates where practicable or rates offered by other financial institutions for loans with similar characteristics. The fair value of floating rate placements, fixed rate placements with less than six months to maturity and overnight deposits is considered to approximate to their carrying amount.

Loans and advances to customers

The Group provides loans of varying rates and maturities to customers. The fair value of loans with variable interest rates is considered to approximate to carrying value as the interest rate can be moved in line with market conditions. For loans with fixed interest rates, fair value was estimated by discounting cash flows using market rates or rates normally offered by the Group. The change in interest rates since the majority of these loans were originated means that their fair value can vary significantly from their carrying value.

However, as the Group's policy is to hedge fixed rate loans in respect of interest rate risk, this does not indicate that the Group has an exposure to this difference in value. However, were the Group to dispose of a portfolio of mortgages, it would be likely the fair value would be lower than disclosed, as there is currently no active market for the sale of mortgage books. The fair value of a loan takes into account credit risk at the balance sheet date.

Loans and advances to customers are categorised as level 3 as unobservable pre-payment rates are applied.

Debt securities classified as loans and receivables

Fair values are based on quoted prices, where available, or by discounting cash flows using market rates.

Available-for-sale financial assets

These are unquoted equity securities held by the Group and relating to participation in banking and credit card operations (refer note 16). They are categorised as level 3 as the fair value of these securities cannot be reliably measured, due to the lack of equivalent instruments with observable prices.

Other assets and liabilities – trade debtors/creditors, accrued income and accrued interest

Fair value is deemed to approximate the carrying value.

Deposits from banks and customer deposits

Fair values of deposit liabilities repayable on demand or with variable interest rates are considered to approximate to carrying value. The fair value of fixed interest deposits with less than six months to maturity is their carrying amount. The fair value of all other deposit liabilities was estimated by discounting cash flows, using market rates or rates currently offered by the Group for deposits of similar remaining maturities.

Debt securities in issue

Fair values are based on quoted prices where available or by discounting cash flows using market rates.

Notes to the consolidated financial statements

Note 34: Fair value of financial assets and liabilities (continued)

Fair value of financial assets and liabilities recognised at fair value

The following table summarises the fair values of those financial assets and liabilities recognised at fair value, by the level in the fair value hierarchy into which each fair value measurement is categorised. The accounting policy in note 1 sets out the key principles for estimating the fair values of financial instruments.

2015	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets				
Derivative financial instruments	**–**	**82.3**	**–**	**82.3**
Available-for-sale financial assets	**1,233.3**	**59.0**	**3.3**	**1,295.6**
Financial liabilities				
Derivative financial instruments	**–**	**156.0**	**–**	**156.0**

2014	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets				
Derivative financial instruments	–	101.2	–	101.2
Available-for-sale financial assets	1,539.6	–	–	1,539.6
Financial liabilities				
Derivative financial instruments	–	228.2	–	228.2

Level 1 Valuations

The fair value of debt securities categorised as available-for-sale financial assets is derived from unadjusted quoted prices in an active market.

Level 2 Valuations

The fair values of derivative instruments are calculated by discounted cash flow models using yield curves that are based on observable market data or are based on valuations obtained from counterparties.

The fair value of level 2 available-for-sale securities are calculated using valuation techniques, including discounted cash flow models.

Level 3 Valuations

This represents the Group's best estimate of the value of its equity investment in Visa Europe Limited. Management has assessed that a reliable estimate of fair value is possible at the year end, following correspondence from Visa Inc. of the consideration expected to be received by the Group from its proposed acquisition of Visa Europe Limited, expected to complete in 2016.

The Group's share of the sale proceeds will comprise upfront consideration and preferred stock. The preferred stock is convertible into Class A common stock, at a future date, subject to the satisfaction of certain conditions. The Group may be entitled to additional deferred consideration four years post completion of the sale, contingent on a number of variable factors including the performance of Visa over that period.

The most significant unobservable input to the valuation is the discount applied to the value of the preferred stock to reflect the risks of future reduction in conversion to Visa Inc. Class A common stock and restrictions on transferability.

Notes to the consolidated financial statements

Note 35: Cash flow statements

(a) Change in operating assets

	2015 £m	2014 £m
Changes in loans and advances to customers	**(4,046.2)**	(2,403.6)
Change in derivative financial assets	**18.9**	86.3
Change in other operating assets	**(10.0)**	(13.3)
Change in operating assets	**(4,037.3)**	(2,330.6)

(b) Change in operating liabilities

	2015 £m	2014 £m
Change in customer deposits	**2,779.2**	1,244.3
Change in derivative financial liabilities	**(72.2)**	81.1
Change in other operating liabilities	**439.4**	480.2
Change in operating liabilities	**3,146.4**	1,805.6

(c) Non-cash and other items

	2015 £m	2014 £m
Depreciation and amortisation	**19.6**	14.8
Gain on sale of subsidiary	**–**	(4.5)
Other non-cash items	**42.8**	(143.1)
Total non-cash and other items	**62.4**	(132.8)

(d) Analysis of cash and cash equivalents as shown in the balance sheet

	2015 £m	2014 £m
Cash and balances at central banks	**888.6**	851.3
Less: mandatory reserve deposits[1]	**(41.7)**	(38.0)
	846.9	813.3
Loans and advances to banks	**614.5**	720.5
Total cash and cash equivalents	**1,461.4**	1,533.8

1 Mandatory reserves with central banks are not available for use in day to day operations .

Notes to the consolidated financial statements

Note 36: Capital resources

Capital is a regulatory measure held by the Group to protect its depositors, to cover inherent risks in a normal and stressed operating environment and to support its business strategy against losses, inherent risks and stress events. In assessing the adequacy of its capital resources, the Group considers its risk appetite, the material risks to which it is exposed and the appropriate strategies required to manage those risks.

The Group manages capital in accordance with prudential rules issued by the PRA and FCA, in line with the EU Capital Requirements Directive (referred to as CRD IV) which implements Basel III in Europe. CRD IV legislation became effective from 1 January 2014.

The Group is committed to maintaining a strong capital base and has complied with all capital requirements set by the regulators throughout the year.

The tables below and on the following page analyse the composition of the regulatory capital resources of the Group on a CRD IV basis in both 2015 and 2014. Throughout 2014, transitional rules for calculating capital under CRD IV were in place and capital resources under those transitional rules were disclosed in the 2014 Annual Report and Accounts.

Own funds

	2015 £m	2014 £m
Common Equity Tier 1		
Share capital and share premium account	**654.6**	654.6
Other equity instruments	**156.5**	156.5
Other reserves	**(15.6)**	(1.8)
Retained earnings	**544.8**	434.5
Total equity	**1,340.3**	1,243.8
Regulatory capital adjustments (unaudited)		
Deconsolidation of non regulated companies	**4.5**	4.1
Expected distribution on Additional Tier 1 securities	**(2.1)**	(2.1)
Expected distribution on ordinary shares	**(13.7)**	–
Other equity instruments	**(156.5)**	(156.5)
Cash flow hedge reserve	**15.3**	8.8
Intangible assets	**(64.4)**	(46.1)
Excess of expected loss over impairment	**(35.4)**	(33.4)
Deferred tax on tax losses carried forward	**(18.0)**	(38.1)
Common Equity Tier 1 capital (unaudited)	**1,070.0**	980.5
Additional Tier 1 securities	**156.5**	156.5
Total Tier 1 capital (unaudited)	**1,226.5**	1,137.0
Tier 2 capital (unaudited)		
General credit risk adjustments	**7.6**	5.9
Total Tier 2 capital	**7.6**	5.9
Total own funds (unaudited)	**1,234.1**	1,142.9

Notes to the consolidated financial statements

Note 36: Capital resources (continued)

Movements in Common Equity Tier 1 capital are summarised below.

(unaudited)	2015 £m	2014 £m
Common Equity Tier 1 capital at 1 January	**980.5**	808.9
Movement in retained earnings	**110.3**	15.5
Net impact of share capital issue	**–**	145.4
Movement in available-for-sale reserve	**(7.3)**	0.5
Movement in expected distribution on Additional Tier 1 securities	**–**	(2.1)
Movement in expected distribution on ordinary shares	**(13.7)**	–
Exclude losses from non regulated companies	**0.4**	0.6
Movement in intangible assets	**(18.3)**	(20.1)
Movement in excess of expected loss over impairment	**(2.0)**	7.7
Movement in deferred tax on tax losses carried forward	**20.1**	24.1
Common Equity Tier 1 capital at 31 December	**1,070.0**	980.5

Risk-weighted assets – Pillar 1

(unaudited)	2015 £m	2014 £m
Retail mortgages	**3,952.9**	3,489.7
Retail unsecured lending	**1,192.7**	830.0
Treasury	**229.0**	221.7
Other assets	**196.3**	175.0
Credit valuation adjustments	**14.3**	13.7
Operational risk	**525.2**	430.5
Total risk-weighted assets	**6,110.4**	5,160.6

The Group calculates its capital requirement for mortgages on an Internal Ratings Based approach, and on the Standardised Basis for credit cards and other assets.

Capital ratios

Capital ratios are calculated as the capital measure shown divided by the total risk-weighted assets of the Group.

(unaudited)	2015 %	2014 %
Common Equity Tier 1 ratio	**17.5%**	19.0%
Tier 1 ratio	**20.1%**	22.0%
Total capital ratio	**20.2%**	22.1%

Notes to the consolidated financial statements

Note 37: Related party transactions

(a) Key Management Personnel

Key Management Personnel refer to the Executive Team of the Virgin Money Group, Non-Executive Directors and Directors of subsidiary companies.

	2015 £m	2014 £m
Compensation		
Salaries and other short-term benefits	**8.2**	6.3
Amounts received under long-term incentive plans	**–**	1.2
Share based payments (Refer note 7)	**12.3**	10.2
Post-employment benefits	**0.9**	0.6
Total compensation	**21.4**	18.3

Aggregate contributions in respect of Key Management Personnel to defined contribution pension schemes £0.9 million (2014: £0.6 million).

	2015 £m	2014 £m
Deposits		
At 1 January	**1.1**	0.9
Placed	**1.8**	0.4
Withdrawn	**(0.7)**	(0.2)
Deposits outstanding at 31 December	**2.2**	1.1

Deposits placed by Key Management Personnel attracted interest rates of up to 2.8% (2014: 2.8 %). At 31 December 2015, the Group did not provide any guarantees in respect of Key Management Personnel (2014: none).

At 31 December 2015, transactions, arrangements and agreements entered into by the Group's banking subsidiaries with Key Management Personnel included amounts outstanding in respect of loans and credit card transactions of £0.3 million with 5 Key Management Personnel (2014: £nil with 4 Key Management Personnel).

Notes to the consolidated financial statements

Note 37: Related party transactions (continued)

(b) Subsidiaries

Transactions and balances with subsidiaries have been eliminated on consolidation. A full list of the company's subsidiaries and SPVs included within the consolidation is provided in note 3 to the parent company financial statements.

(c) Other transactions

Transaction value at year end:	2015 £m	2014 £m
Trademark licence fees to Virgin Enterprises Ltd	**5.1**	4.3
Virgin Atlantic Airways	**–**	2.8
Dividend payment to Virgin Group Holdings Limited	**2.2**	–
Other costs to Virgin Management Group Companies	**0.4**	0.2

Balance outstanding at year end:	2015 £m	2014 £m
Trademark licence fees to Virgin Enterprises Ltd	**(0.4)**	(0.4)
Virgin Atlantic Airways	**–**	–
Dividend payment to Virgin Group Holdings Limited	**–**	–
Other costs to Virgin Management Group Companies	**(0.1)**	(0.1)

Trademark licence fees to Virgin Enterprises Limited

Licence fees are payable to Virgin Enterprises Limited for the use of the Virgin Money brand trademark.

Virgin Atlantic Airways

The Group incurs credit card commissions and air mile charges to Virgin Atlantic Airways Limited (VAA) in respect of an agreement between the two parties. Prior to 2014, there was a tripartite agreement between the Group, VAA and MBNA for the credit card commission and air mile charges to VAA.

Dividend payment to Virgin Group Holdings Limited

The Group made a dividend payment of £2.2 million to Virgin Group Holdings Limited in October 2015, which represented that company's proportionate share of the total interim dividend (refer note 11).

Other costs to Virgin Management Group Companies

These costs include transactions with other companies in the Virgin Group.

It is anticipated that Sapphire Cards Limited (formerly Virgin Money Cards Limited), which is no longer part of the Group, will benefit from the surrender of tax losses by the Virgin Group in the years 2009 to 2011. This anticipated transaction is considered to meet the definition of a related party transaction (refer note 9).

The Group incurs credit card point of sale discount fees to Virgin Holidays Limited.

A number of banking transactions are entered into with related parties as part of normal banking business. These include deposits.

Note 38: Events after balance sheet date

On 25 January 2016, the Group raised £803.0 million from institutional investors through the issuance of Residential Mortgage Backed Securities in the Gosforth Funding 2016-1 transaction.

Notes to the consolidated financial statements

Note 39: Future accounting developments

A number of new accounting standards and amendments to accounting standards have been issued by the IASB, however have not been endorsed by the European Union. Those which may be relevant to the Group are set out below.

Pronouncement	Nature of change	IASB effective date
IFRS 9 'Financial Instruments'	IFRS 9 'Financial Instruments', published in July 2014, replaces the existing guidance in IAS 39 'Financial Instruments: Recognition and Measurement'. IFRS 9 is split over 3 phases: Phase 1 includes revised guidance on the classification and measurement of financial instruments. Financial assets will be classified and measured based on the business model under which they are held and the characteristics of their contractual cash flows. Financial liabilities designated under the fair value option will be required to generally present fair value changes that are attributable to the liability's credit risk in other comprehensive income rather than profit or loss. Phase 2 is a new expected credit loss model for calculating impairment on financial assets. Under this approach, it is no longer necessary for a credit event to have occurred before credit losses are recognised. Instead, the Group will always account for expected credit losses and changes in those expected credit losses. Phase 3 is the new general hedge accounting requirements. These requirements aim to more closely align hedge accounting with the Group's risk management strategy. The work on macro hedging by the IASB is still at a preliminary stage and has not yet been issued as part of the finalised standard. A project team has been mobilised to begin work on assessing the impact of IFRS 9 across the Group, with particular emphasis on phase 2 – the new impairment expected credit loss model. At this stage a full assessment of the impact of IFRS 9 has not been made by the Group. The Group is on track to successfully deliver the changes required to adopt IFRS 9 on 1 January 2018 (subject to EU endorsement).	1 January 2018 (has not been EU endorsed)
IFRS 15 'Revenue from Contracts with Customers'	Current revenue recognition accounting standards have led to inconsistencies in accounting for similar transactions and inadequate disclosures. IFRS 15 specifies comprehensive principles on whether, how much and when an entity should recognise revenue arising from customer contracts. In addition, extensive disclosure requirements have been introduced to provide more informative and relevant disclosures, particularly around estimates and judgements. The Group is reviewing the requirements of the new standard to determine its effect on its financial reporting.	1 January 2018 (has not been EU endorsed)
IFRS 16 'Leases'	This standard replaces IAS 17 'Leases' and will result in most leases for lessees being brought on to the Balance Sheet under a single lease model, removing the distinction between finance and operating leases. It requires a lessee to recognise a 'right-of-use' asset and a lease liability. Lessor accounting remains largely unchanged. The Group is reviewing the requirements of the new standard to determine its effect on its financial reporting.	1 January 2019 (has not been EU endorsed)

Notes to the consolidated financial statements

Note 40: Country by country reporting

The Capital Requirements (Country by Country Reporting) Regulations came into effect on 1 January 2014 and place certain reporting obligations on financial institutions within CRD IV.

All companies consolidated within the Group's financial statements are UK registered entities.

The activities of the Group are described in the Strategic Report.

	UK
Number of employees (average FTE)	2,824
Turnover (total income)	£521.9m
Pre tax profit	£138.0m
Corporation tax paid	£5.0m
Public subsidies received	£0.0m

The Group received no public subsidies during the year.

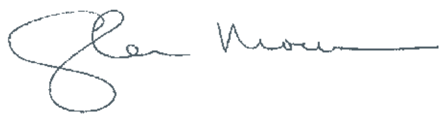
Parent Company balance sheet

As at 31 December

	Notes	2015 £ million	2014 £ million
Assets			
Loans and advances to banks	2	**103.0**	127.8
Derivative financial instruments		**1.5**	1.1
Investment in subsidiary undertakings	3	**1,127.6**	1,107.6
Deferred tax assets	4	**0.1**	0.2
Other assets	5	**16.4**	16.3
Total assets		**1,248.6**	1,253.0
Equity and liabilities			
Liabilities			
Deposits from banks		**1.6**	1.0
Derivative financial instruments		**0.7**	0.2
Other liabilities	6	**164.7**	165.9
Total liabilities		**167.0**	167.1
Equity			
Share capital and share premium	7	**654.6**	654.6
Other equity instruments	8	**156.5**	156.5
Retained earnings	9	**270.5**	274.8
Total equity		**1,081.6**	1,085.9
Total equity and liabilities		**1,248.6**	1,253.0

The accompanying notes are an integral part of the parent company financial statements.

The financial statements were approved and authorised for issue by the Board and were signed on its behalf on 1 March 2016.



Glen Moreno
Chairman

Jayne-Anne Gadhia CBE
Chief Executive

Parent Company statement of changes in equity

As at 31 December

	Share capital and share premium £ million	Other equity instruments £ million	Retained earnings £ million	Total equity £ million
Balance as at 1 January 2015	**654.6**	**156.5**	**274.8**	**1,085.9**
Loss for the year	**–**	**–**	**(3.1)**	**(3.1)**
Total comprehensive expense for the year	**–**	**–**	**(3.1)**	**(3.1)**
Transactions with equity holders				
Capital contribution – share based payments	**–**	**–**	**20.0**	**20.0**
Purchase of own shares	**–**	**–**	**(5.0)**	**(5.0)**
Distribution to Additional Tier 1 noteholders	**–**	**–**	**(12.6)**	**(12.6)**
Group relief attributable to Tier 1 Securities	**–**	**–**	**2.6**	**2.6**
Dividends paid to ordinary shareholders	**–**	**–**	**(6.2)**	**(6.2)**
Balance as at 31 December 2015	**654.6**	**156.5**	**270.5**	**1,081.6**

	Share capital and share premium £ million	Other equity instruments £ million	Retained earnings £ million	Total equity £ million
Balance as at 1 January 2014	509.2	–	325.4	834.6
Loss for the year	–	–	(57.4)	(57.4)
Total comprehensive expense for the year	–	–	(57.4)	(57.4)
Transactions with equity holders				
Capital contribution – share based payments	–	–	17.1	17.1
Issue of ordinary shares (net)	145.4	–	–	145.4
Issue of Additional Tier 1 securities (net)	–	156.5	–	156.5
Distribution to Additional Tier 1 noteholders	–	–	(3.2)	(3.2)
Distribution to Non-core Tier 1 noteholders	–	–	(9.2)	(9.2)
Group relief attributable to Tier 1 Securities	–	–	2.1	2.1
Balance as at 31 December 2014	654.6	156.5	274.8	1,085.9

Parent Company cash flow statement

For the year ended 31 December

	Notes	**2015 £ million**	2014 £ million
Loss before taxation		**(3.8)**	(57.4)
Adjustments for:			
Changes in operating assets	12(a)	**–**	1.7
Changes in operating liabilities	12(b)	**(0.7)**	(0.9)
Non-cash and other items	12(c)	**3.4**	57.1
Movement in amounts due to group undertakings		**0.6**	28.9
Unrealised movement on derivatives		**–**	(2.0)
Loss on sale of subsidiaries		**–**	0.4
Net cash (used in)/provided by operating activities		**(0.5)**	27.8
Net cash inflow from investing activities			
Net cash flow from disposal of Church House Trust		**–**	11.5
Net cash provided by investing activities		**–**	11.5
Net cash (outflow)/inflow from financing activities			
Distribution to Non-core Tier 1 loan noteholders		**–**	(17.0)
Repayment of Non-core Tier 1 notes		**–**	(154.5)
Issue of Additional Tier 1 securities (net)		**–**	156.5
Distribution to Additional Tier 1 security holders		**(12.6)**	(3.2)
Proceeds from share issues (net)		**–**	145.4
Purchase of own shares		**(5.0)**	–
Movements in amounts from group undertakings		**(0.5)**	(0.5)
Dividends paid on ordinary shares		**(6.2)**	–
Payment of additional Northern Rock consideration		**–**	(50.0)
Net cash (used in)/provided by financing activities		**(24.3)**	76.7
Change in cash and cash equivalents		**(24.8)**	116.0
Cash and cash equivalents at beginning of year		**127.8**	11.8
Cash and cash equivalents at end of year	2	**103.0**	127.8

The accompanying notes are an integral part of the parent company financial statements.

Notes to the Parent Company financial statements

Note 1: Basis of preparation

1.1 Basis of preparation

The financial statements of Virgin Money Holdings (UK) plc, (the Parent Company, the Company), which should be read in conjunction with the Group Directors' Report, have been prepared on a going concern basis in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and with those parts of the Companies Act 2006 applicable to companies reporting under IFRS. No individual statement of comprehensive income is presented for the Company, as permitted by Section 408(4) of the Companies Act 2006.

1.2 Basis of measurement

The financial statements have been prepared under the historical cost convention as modified by the revaluation of derivative financial instruments and other assets held at fair value through profit or loss.

The preparation of the financial statements in conformity with IFRS requires Management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

The accounting policies of the Company are the same as those of the Group which are set out in note 1 of the consolidated financial statements except that the Company has no policy in respect of consolidation and investments in subsidiaries which are carried at historical cost, less any provision for impairment. These accounting policies have been applied consistently to all periods presented in these financial statements.

Note 2: Loans and advances to banks

	2015 £m	2014 £m
Money market placements with banks	**97.1**	120.8
Other lending to banks	**5.9**	7.0
Total	**103.0**	127.8

Note 3: Investment in subsidiaries

	2015 £m	2014 £m
At 1 January	**1,107.6**	1,119.0
Sale of Church House Trust Limited	**–**	(28.5)
Capital contribution – share based payments	**20.0**	17.1
At 31 December	**1,127.6**	1,107.6

Notes to the Parent Company financial statements

Note 3: Investment in subsidiaries (continued)

The following were subsidiaries of the Company or SPVs controlled by the Company in accordance with note 1.5 to the consolidated financial statements:

Name	Class of Share	Holding
Direct holdings		
Virgin Money plc	Ordinary	100%
Virgin Money Personal Financial Service Limited	Ordinary	100%
Virgin Money Unit Trust Managers Limited	Ordinary	100%
Virgin Money Management Services Limited	Ordinary	100%
Virgin Money Giving Limited	Ordinary	100%
Challenger (Norwich) Limited[1]	Ordinary	100%
Indirect holdings		
Virgin Card Limited[1]	Ordinary	100%
Virgin Money Nominees Limited*	Ordinary	100%
Northern Rock Limited*	Ordinary	100%
Northern Rock (Guernsey) Limited[2]	Ordinary	100%

Special purpose vehicles	Nature of business
Gosforth Funding plc [3]	Issue of securitised notes
Gosforth Funding 2011-1 plc	Issue of securitised notes
Gosforth Funding 2012-1 plc	Issue of securitised notes
Gosforth Funding 2012-2 plc	Issue of securitised notes
Gosforth Funding 2014-1 plc	Issue of securitised notes
Gosforth Funding 2015-1 plc	Issue of securitised notes
Gosforth Funding 2016-1 plc	Issue of securitised notes
Gosforth Mortgages Trustee 2011-1 Limited	Trust
Gosforth Mortgages Trustee 2012-1 Limited	Trust
Gosforth Mortgages Trustee 2012-2 Limited	Trust
Gosforth Mortgages Trustee 2014-1 Limited	Trust
Gosforth Mortgages Trustee 2015-1 Limited	Trust
Gosforth Mortgages Trustee 2016-1 Limited	Trust
Gosforth Holdings Limited[4]	Holding company
Gosforth Holdings 2011-1 Limited	Holding company
Gosforth Holdings 2012-1 Limited	Holding company
Gosforth Holdings 2012-2 Limited	Holding company
Gosforth Holdings 2014-1 Limited	Holding company
Gosforth Holdings 2015-1 Limited	Holding company
Gosforth Holdings 2016-1 Limited	Holding company

* Dormant companies.

1 Dormant company, strike off application submitted.

2 Dissolved 2 January 2015.

3 Dissolved 30 March 2015.

4 Dissolved 27 January 2015.

Notes to the Parent Company financial statements

Note 4: Deferred tax assets

The Directors conclude that net deferred tax assets of £0.1 million (2014: £0.2 million) should be recognised at the balance sheet date. This is based on their interpretation of the timing and level of reversal of existing taxable temporary differences, in line with relevant accounting standards.

	2015 £m	2014 £m
Change in accounting basis on adoption of IFRS	**0.1**	0.2
Recognised deferred tax assets	**0.1**	0.2

The Company is expected to generate sufficient taxable profits in future periods to recover these assets. The Company has not recognised deferred tax assets in respect of gross unused tax losses of £31.1 million (2014: £28.7 million).

Note 5: Other assets

	2015 £m	2014 £m
Amounts owed from subsidiary undertakings	**12.8**	12.3
Group relief owed from related parties	**3.3**	3.2
Other	**0.3**	0.8
Total	**16.4**	16.3

Note 6: Other liabilities

	2015 £m	2014 £m
Other creditors	**–**	1.8
Amounts owed to subsidiary undertakings	**164.7**	164.1
Total	**164.7**	165.9

Note 7: Share capital and share premium

Details of the Company's share capital and share premium are given in note 29 of the consolidated financial statements.

Note 8: Other equity instruments

Details of the Company's other equity instruments are given in note 30 of the consolidated financial statements.

Notes to the Parent Company financial statements

Note 9: Retained earnings

Retained earnings comprise:

	Subsidiary contribution £m	Investment in own shares £m	Retained profits £m	Total £m
At 1 January 2014	1.4	(6.2)	330.2	325.4
Loss for the year	–	–	(57.4)	(57.4)
Distributions to Tier 1 security holders (net of tax)	–	–	(10.3)	(10.3)
Award of shares from own shares	–	4.1	(4.1)	–
Capital contribution – share based payments	17.1	–	–	17.1
As at 31 December 2014	**18.5**	**(2.1)**	**258.4**	**274.8**
Loss for the year	**–**	**–**	**(3.1)**	**(3.1)**
Dividends paid to ordinary shareholders	**–**	**–**	**(6.2)**	**(6.2)**
Distributions to Tier 1 security holders (net of tax)	**–**	**–**	**(10.0)**	**(10.0)**
Purchase of own shares	**–**	**(5.0)**	**–**	**(5.0)**
Award of shares from own shares	**–**	**4.2**	**(4.2)**	**–**
Capital contribution – share based payments	**20.0**	**–**	**–**	**20.0**
As at 31 December 2015	**38.5**	**(2.9)**	**234.9**	**270.5**

Employee benefit trust

As part of an arrangement to allow holders of certain shares in the Company an opportunity to access some of the value increase in the Virgin Money Group since the original grant date, the Company established an EBT in 2011. For further details refer to note 32 in the consolidated financial statements.

Notes to the Parent Company financial statements

Note 10: Analysis of financial assets and financial liabilities by measurement basis

2015	Financial liabilities at amortised cost £m	Loans and receivables £m	Derivatives not in IAS 39 hedges £m	Total £m
Financial assets				
Loans and advances to banks	–	103.0	–	103.0
Derivative financial instruments	–	–	1.5	1.5
Amounts owed from subsidiary undertakings	–	12.8	–	12.8
Total financial assets	–	115.8	1.5	117.3
Non financial assets				1,131.3
Total assets				1,248.6
Financial liabilities				
Deposits from banks	1.6	–	–	1.6
Derivative financial instruments	–	–	0.7	0.7
Amounts owed to subsidiary undertakings	164.7	–	–	164.7
Total financial liabilities	166.3	–	0.7	167.0
Non financial liabilities				–
Total liabilities				167.0
Equity				1,081.6
Total liabilities and equity				1,248.6

2014	Financial liabilities at amortised cost £m	Loans and receivables £m	Derivatives not in IAS 39 hedges £m	Total £m
Financial assets				
Loans and advances to banks	–	127.8	–	127.8
Derivative financial instruments	–	–	1.1	1.1
Amounts owed from subsidiary undertakings	–	12.3	–	12.3
Total financial assets	–	140.1	1.1	141.2
Non financial assets				1,111.8
Total assets				1,253.0
Financial liabilities				
Deposits from banks	1.0	–	–	1.0
Derivative financial instruments	–	–	0.2	0.2
Amounts owed to subsidiary undertakings	164.1	–	–	164.1
Other creditors – accrued interest	0.1	–	–	0.1
Total financial liabilities	165.2	–	0.2	165.4
Non financial liabilities				1.7
Total liabilities				167.1
Equity				1,085.9
Total liabilities and equity				1,253.0

Notes to the Parent Company financial statements

Note 11: Fair value of financial assets and financial liabilities recognised at cost

	Level 1 £m	Level 2 £m	Level 3 £m	2015 Total fair value £m	2015 Total carrying value £m	2014 Total fair value £m	2014 Total carrying value £m
Financial assets							
Loans and advances to banks	–	**103.0**	–	**103.0**	**103.0**	127.8	127.8
Amounts due from subsidiary undertakings	–	**12.8**	–	**12.8**	**12.8**	12.3	12.3
Financial liabilities							
Amounts owed to subsidiary undertakings	–	**164.7**	–	**164.7**	**164.7**	164.1	164.1
Deposits from banks	–	**1.6**	–	**1.6**	**1.6**	1.0	1.0
Other liabilities – accrued interest	–	–	–	–	–	0.1	0.1

The Company has £0.8 million (2014: £0.9 million) of net derivative financial instruments classified as level 2 in the fair value hierarchy.

Note 12: Cash flow statements

(a) Change in operating assets

	2015 £m	2014 £m
Change in derivative financial assets	**(0.4)**	1.1
Change in other operating assets	**0.4**	0.6
Change in operating assets	**–**	1.7

(b) Change in operating liabilities

	2015 £m	2014 £m
Change in derivative financial liabilities	**0.5**	(1.8)
Change in other operating liabilities	**(1.2)**	0.9
Change in operating liabilities	**(0.7)**	(0.9)

(c) Non-cash and other items

	2015 £m	2014 £m
Other non-cash items	**3.4**	57.1
Total non-cash and other items	**3.4**	57.1

Notes to the Parent Company financial statements

Note 13: Related party transactions

Key Management Personnel

The Key Management personnel of the Company are Key Management personnel of the Group, with relevant disclosures given in note 37 to the consolidated financial statements. The Company has no employees (2014: nil).

As discussed in note 7 of the consolidated financial statements, the Group provides share-based compensation to employees through a number of schemes; these are all in relation to shares in the Company and the cost of providing those benefits is not recharged to the employing company.

Other transactions

	Transaction value Year ended 31 December		Balance outstanding at 31 December	
	2015 £m	2014 £m	**2015 £m**	2014 £m
Recharges and trading balances owed (by)/to subsidiaries	**0.8**	0.8	**(2.6)**	12.2
Loans from subsidiaries	**3.8**	3.6	**151.2**	136.4
Dividend payment to Virgin Group Holdings Limited	**2.2**	–	**–**	–

Glossary

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 III	Global regulatory standard on Bank Capital Adequacy, Stress Testing and Market and Liquidity proposed by the Basel Committee on Banking Supervision in 2010. See also CRD IV.
Basis Point (bps)	One hundredth of a per cent (0.01%). 100 basis points is 1%. Used when quoting movements in interest rates or yields.
Capital at Risk	Approach set out for the quantification of interest rate risk expressed as present value of the impact of the sensitivity analysis on the Group's capital.
CASS	Client Assets Sourcebook – included in the FCA Handbook and sets out the requirements with which firms must comply when holding or controlling client assets.
Certificates of Deposit	Bearer negotiable instruments acknowledging the receipt of a fixed term deposit at a specified interest rate.
Charge Off	Charge off occurs on outstanding credit card balances which are deemed irrecoverable. This involves the removal of the balance and associated provision from the balance sheet with any remaining outstanding balance recognised as a loss.
Common Equity Tier 1 Capital	The highest quality form of capital under CRD IV that comprises common shares issued and related share premium, retained earnings and other reserves excluding the cash flow hedging reserve, less specified regulatory adjustments.
Cost of Capital	The cost of funds used to finance the business including distributions to AT1 security holders.
Cost of Risk	Cost of risk is defined as impairment charges divided by simple average gross loans for a given period.
Cost:Income Ratio	Operating expenses compared to total income. The Group calculates this ratio using the 'underlying basis' which is the basis on which financial information is reported internally to management.
CRD IV	In June 2013, the European Commission published legislation for a Capital Requirements Directive (CRD) and Capital Requirements Regulation (CRR) which form the CRD IV package. The package implements the Basel III proposals in addition to the inclusion of new proposals on sanctions for non-compliance with prudential rules, corporate governance and remuneration. The rules are implemented in the UK via the PRA policy statement PS7/13 and came into force from 1 January 2014, with certain sections subject to transitional phase in.
Credit Default Swap	A credit default swap is a type of credit derivative. It is an arrangement whereby the credit risk of an asset (the reference asset) is transferred from the buyer to the seller of protection. The entity selling protection receives premium or interest-related payments in return for contracting to make payments to the protection buyer upon a defined credit event. Credit events normally include bankruptcy, payment default on a reference asset or assets, or downgrades by a rating agency.
Credit Enhancements	Techniques that improve the credit standing of financial obligations; generally those issued by a structured entity in a securitisation.
Credit Spread	The credit spread is the yield spread between the securities with the same currency and maturity structure but with different associated credit risks, with the yield spread rising as the credit rating worsens. It is the premium over the benchmark or risk-free rate required by the market to take on a lower credit quality.
Credit Valuation Adjustments	These are adjustments to the fair values of derivative assets to reflect the creditworthiness of the counterparty.
Cross-currency Swaps	An arrangement in which two parties exchange specific principal amounts in different currencies at inception and subsequently interest payments on the principal amounts.
Debt Securities	Debt securities are assets held by the Group representing certificates of indebtedness of credit institutions, public bodies or other undertakings, excluding those issued by Central Banks.
Default	Default occurs where a borrower has missed 6 months of mortgage repayments or 3 months of credit card repayments, or, the borrower is deemed to be unlikely to repay their loan. The definition of unlikely to repay includes those loans where: the property has been taken into possession; loans that have been modified in the form of a "Rescue Solution" debt management plan; loans where the customer is at least one month in arrears and they have active public information at the credit bureau.
Earnings at Risk	Approach set out for the quantification of interest rate risk expressed as the impact of the sensitivity analysis on the change to net interest income.
Expected Loss	This is the amount of loss that can be expected by the Group calculated in accordance with PRA rules. In broad terms it is calculated by multiplying the Probability of Default by the Loss Given Default by the Exposure at Default.
Exposure at Default (EAD)	An estimate of the amount expected to be owed by a customer at the time of a customer's default.
Forbearance	Forbearance takes place when a concession is made on the contractual terms of a loan in response to borrowers' financial difficulties; or for where the contractual terms have been cancelled for credit cards. Forbearance options are determined by assessing the customer's personal circumstances.

Glossary

Full Time Equivalent (FTE)	A full time employee is one that works a standard five day week. The hours worked by part time employees are measured against this standard and accumulated along with the number of full time employees and counted as full time equivalents.
Funding for Lending Scheme (FLS)	The Bank of England launched the Funding for Lending scheme in 2012 to allow banks and building societies to borrow from the Bank of England at cheaper than market rates for up to four years. This was designed to increase lending to businesses by lowering interest rates and increasing access to credit.
Funding Risk	The inability to raise and maintain sufficient funding in quality and quantity to support the delivery of the business plan.
Help to Buy	'Help to Buy' was formed as part of the 2013 budget announcement by the Government and is part of a package of measures designed to increase the availability of low-deposit mortgages for credit worthy households and to boost the supply of new housing.
Impaired Assets	Loans that are in arrears, or where there is objective evidence of impairment, and where the carrying amount of the loan exceeds the expected recoverable amount.
Impairment Allowance	Impairment allowances are a provision held on the balance sheet as a result of the raising of a charge against profit for the incurred loss inherent in the lending book. An impairment allowance may either be individual or collective.
Impairment Losses	An impairment loss is the reduction in value that arises following an impairment review of an asset that determined that the asset's value is lower than its carrying value. For impaired financial assets measured at amortised cost, impairment losses are the difference between the carrying value and the present value of estimated future cash flows, discounted at the asset's original effective interest rate.
Interest Rate Risk	The risk of a reduction in the value of earnings or assets resulting from an adverse movement in interest rates.
Interest Rate Risk in the Banking Book (IRRBB)	The risk to interest income arising from a mismatch between the duration of assets and liabilities that arises in the normal course of business activities.
Internal Capital Adequacy Assessment Process (ICAAP)	The Group's own assessment of the levels of capital that it needs to hold in respect of its regulatory capital requirements (for credit, market and operational risks) and for other risks including stress events as they apply on a solo level and on a consolidated level.
Leverage Ratio	Total Tier 1 Capital expressed as a percentage of Total assets (adjusted in accordance with CRD IV).
Liquidity Coverage Ratio (LCR)	Stock of high quality liquid assets as a percentage of expected net cash outflows over the following 30 days.
Liquidity Risk	The inability to accommodate liability maturities and withdrawals, fund asset growth, and otherwise meet the Group's contractual obligations to make payments as they fall due.
Loan-to-Deposit Ratio	The ratio of loans and advances to customers net of allowance for impairment divided by customer deposits (each excluding repurchase agreements). Fair value of portfolio hedging is excluded from this calculation.
Loan-to-Value Ratio	The amount of a secured loan as a percentage of the appraised value of the security e.g. the outstanding amount of mortgage loan as a percentage of the property's value.
Loss Emergence Period	The loss emergence period is the estimated period between impairment occurring and the loss specifically identified and evidenced by the establishment of an appropriate impairment allowance.
Loss Given Default (LGD)	The estimated loss that will arise if a customer defaults. It is calculated after taking account of credit risk mitigation and includes the cost of recovery.
Master Netting Agreement	An agreement between two counterparties that have multiple derivative contracts with each other that provides for the net settlement of all contracts through a single payment, in a single currency, in the event of default on, or termination of, any one contract.
Net Interest Income	The difference between interest received on assets and interest paid on liabilities.
Net Interest Margin (NIM)	Net interest income as a percentage of average interest-earning assets.
Net Stable Funding Ratio (NSFR)	The ratio of available stable funding to required stable funding over a one year time horizon, assuming a stressed scenario. The ratio is required to be 100% with effect from 2018. Available stable funding would include such items as equity capital, preferred stock with a maturity of over 1 year, or liabilities with a maturity of over 1 year.
Option	An option is a contract that gives the holder of the right but not the obligation to buy (or sell) a specified amount of the underlying physical or financial commodity, at a specified price, at an agreed date or over an agreed period.
Percentage Point (pp)	Unit for measuring the difference of two percentages. A change from 1% to 2% is 1 percentage point.
Pillar 1	The part of CRD IV that sets out the process by which regulatory capital requirements should be calculated for credit, market and operational risk.
Pillar 2	The part of CRD IV that 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	The part of CRD IV that sets out the information banks must disclose in relation to their risks, the amount of capital required to absorb them, and their approach to risk management. The aim is to strengthen market discipline.
Probability of Default (PD)	The probability of a customer becoming six months or more past due on their mortgage obligations, or three month past due for credit cards, over a defined outcome period. The outcome period varies for assessment of capital requirements and for assessment of provisions.
Repurchase Agreements (Repos)	An agreement where one party, the seller, sells a financial asset to another party, the buyer, at the same time the seller agrees to reacquire and the buyer to resell the asset at a later date. From the seller's perspective such agreements are repurchase agreements (repos) and from the buyer's reverse repurchase agreements (reverse repos).
Retail Distribution Review	Consumer protection strategy of the FCA.
Return on Equity	Profit attributable to ordinary shareholders divided by average shareholders' equity.
Return on tangible equity	Underlying profit before tax adjusted for distributions to Additional Tier 1 noteholders and tax divided by average tangible equity.
Risk Appetite	The variability in results or key outcomes that the board is willing to accept in support of the Group.
Risk-Weighted Assets	A measure of a bank's assets adjusted for their associated risks. Risk weightings are established in accordance with PRA rules.
Secured Lending	Lending on which the borrower uses collateral such as equity in their home.
Securitisation	Securitisation is a process by which a group of assets, usually loans, are aggregated into a pool, which is used to back the issuance of new securities through an SPV.
Sovereign Exposures	Exposures to central governments and central government departments, central banks and entities owned or guaranteed by the aforementioned.
Standardised Approach	In relation to credit risk, a method for calculating credit risk capital requirements using External Credit Assessment Institutions (ECAI) ratings of obligators (where available) and supervisory risk weights. In relation to operational risk, a method of calculating the operational risk capital requirement by the application of a supervisory defined percentage charge to the gross income of specified business lines.
Stress Testing	Techniques where plausible events are considered as vulnerabilities to ascertain how this will impact the capital resources which are required to be held.
Tangible Equity	A subset of shareholders equity that is not intangible assets.
Tier 1 Capital	A measure of banks financial strength defined by the PRA. It captures Common Equity Tier 1 capital plus other Tier 1 securities in issue, but is subject to a deduction in respect of material holdings in financial companies.
Tier 1 Capital Ratio	Tier 1 capital as a percentage of risk-weighted assets.
Tier 2 Capital	A further component of regulatory capital defined by the PRA. It comprises eligible collective assessed impairment allowances under CRD IV.
Underlying EPS	Underlying profit before tax adjusted for distributions to Additional Tier 1 noteholders and tax divided by the weighted-average number of Ordinary Shares outstanding during the period excluding own shares held in employee benefit trusts or held for trading.
Unsecured Lending	Lending with no collateral held such as credit cards and current account overdrafts.
Virgin	Virgin Group Holdings Limited.
Virgin Money Foundation	A new charitable foundation established by Virgin Money to invest in projects designed to benefit communities in which Virgin Money works.
Virgin Money Trademark Licence Agreement	The agreement under which Virgin Enterprises Limited grants perpetual licence to Virgin Money to use the "Virgin" and "Virgin Money" trademarks.
WLR	WLR IV VM LLC and WLR IV VM II LLC, together major shareholders of the Company.
Write Off	Mortgages: may be written off where the outstanding balance or shortfall from sale of property is deemed irrecoverable. Assets written off will be deducted from the balance sheet. Credit cards: a write off occurs following charge off when all attempts to recover the outstanding balance is exhausted and the account is closed.
Yield Curve	A line that plots the interest rates, at a set point in time, of an asset class or swap rate at varying maturities. This can be used as a gauge to evaluate the future of interest rates.

Abbreviations

AGM	Annual General Meeting
AIL	Ageas Insurance Limited
AT1	Additional Tier 1
BBA	British Bankers Association
BBR	Bank Base Rate
BOE	Bank of England
CET1	Common Equity Tier 1 Capital
CMA	Competition and Markets Authority
CML	Council of Mortgage Lenders
CONC	Consumer Credit Sourcebook
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
CVA	Credit Valuation Adjustment
DTR	Disclosure and Transparency Rules
EBO	Everyone's better off
ECA	Essential Current Account
EPS	Earnings per share
FCA	Financial Conduct Authority
FLS	Funding for Lending Scheme
FPC	Financial Policy Committee
FRC	Financial Reporting Council
FSCS	Financial Services Compensation Scheme
FTP	Funds Transfer Pricing
GHG	Greenhouse Gas
HMRC	Her Majesty's Revenue and Customs
HPI	House Pricing Index
IAS	International Accounting Standards
IASB	International Accounting Standards Board
ICAAP	Internal Capital Adequacy Assessment Process
IFDS	International Financial Data Services Limited
IFRS	International Financial Reporting Standards
ILAA	Individual Liquidity Adequacy Assessment
IPO	Initial Public Offering
ISA	Individual Savings Account
ISDA	International Swaps and Derivatives Association
LIBOR	London Inter-Bank Offered Rate
LTIP	Long-Term Incentive Plan
MTN	Medium Term Note
NPS	Net Promoter Score
OTC	Over the Counter
PCA	Personal Current Account
PRA	Prudential Regulation Authority
RMBS	Residential Mortgage Backed Securities
SME	Small or Medium-sized Enterprise
SPV	Special Purpose Vehicle
TNAV	Tangible net asset value
TSYS	Total System Services, Inc

Shareholder Information

Annual General Meeting

The AGM will be held on 4 May 2016 at the offices of Allen & Overy at One Bishops Square, London, E1 6AD. Further details about the meeting, including the proposed resolutions, can be found in our Notice of AGM which will be issued to shareholders and available on our website in due course.

Shareholder concentration

As of 31 December 2015	Number of shares – millions	Shareholdings	%
Individuals	0.4	560	0.1
Banks & Nominees	262.3	293	59.1
Other companies	169.2	91	38.1
Other corporates	11.8	31	2.7
	443.7	975	100.0

Range of shareholdings:	Number of shares – millions	Shareholdings	%
1-1,000	0.2	585	0.0
1,001-10,000	0.5	125	0.1
10,001-100,000	4.2	107	1.0
100,001-1,000,000	40.5	105	9.1
1,000,001-10,000,000	151.7	49	34.2
>10,000,001	246.6	4	55.6
	443.7	975	100.0

Shareholder Information

Registrar

The Virgin Money share register is maintained by Equiniti Limited. Equiniti is responsible for keeping Virgin Money's register of members up to date and for administering the payment of dividends.

Enquiries

Please contact Equiniti if you have any enquiries about your Virgin Money shareholding, including the following:

- Change of name or address.
- Change of bank account details.
- Loss of share certificate, dividend warrant or tax voucher.
- To obtain a form for dividends to be paid directly to your bank or building society account (tax vouchers will be sent to your registered address unless your request otherwise).
- Request for copies of the report and accounts in alternative formats for shareholders with disabilities.
- Lost or out of date dividend payments.
- Share transfers.
- Information regarding the administration of your shareholding.

UK – **0871 384 2937**
Textphone – **0871 384 2255**
Overseas – **+44 (0)121 415 0857**

Lines are open 8.30am to 5.30pm Monday to Friday (except UK public holidays).

Equinity operates a web-based enquiry and portfolio management service for shareholders www.shareview.co.uk

Address: Equiniti Limited, Aspect House, Spencer Road, Lancing, West Sussex, BN99 6DA.

RECYCLED
Paper made from recycled material
FSC® C022913
FSC
www.fsc.org

This report is printed on Cocoon Silk 130, made from 100% genuine de-inked post-consumer waste and is FSC® certified.

Merrill Corporation Ltd, London

Issued by Virgin Money Holdings (UK) plc.

Registered office:
Jubilee House, Gosforth,
Newcastle upon Tyne NE3 4PL

Registered in England
and Wales no.03087587